Financial Conduct Authority

FINAL NOTICE

To: **Yorkshire Building Society ("YBS")**

Firm Reference Number: **106085**

Address: **Yorkshire House**
Yorkshire Drive
Bradford
BD5 8LJ

Date: **16 June 2014**

1. ACTION

1.1 For the reasons given in this notice, the Authority hereby imposes on YBS a financial penalty of £1,429,000.

1.2 YBS agreed to settle at an early stage of the Authority's investigation. YBS therefore qualified for a 30% Stage 1 discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £2,041,500 on YBS.

2. SUMMARY OF REASONS

2.1 In the period 1 November 2009 to 17 June 2012 ("the Relevant Period"), YBS breached Principle 7 of the Authority's Principles for Businesses ("the Principles") in that it failed to pay due regard to the information needs of its clients and communicate with them in a way which is clear, fair and not misleading. The financial promotions which YBS provided to its customers for the Cliquet Product[1] did not satisfy this requirement.

2.2 The Cliquet Product was designed and issued by Credit Suisse International ("CSI"), but sold to retail investors through third party distributors, including YBS. During the Relevant Period, YBS was the largest distributor of the Cliquet Product, responsible for approximately 75% of the total amount invested in the Cliquet Product. YBS launched and distributed 44 issues of the Cliquet Product during this period. In total, 56,236 customers invested £545,694,211 in these 44 issues. These retail investors were typically unsophisticated investors with limited investment experience and knowledge. Across all distributors, the age profile of the investors was 14.5% under 45, 53% between 45 and 65 and 32.5% over 65.

2.3 Throughout the Relevant Period, YBS prepared and issued its own financial promotions relating to the Cliquet Product which included promotional flyers; branch posters; direct mail letters and web pages (collectively, the "YBS Financial Promotions"). In addition, YBS approved and provided to its customers Product Brochures prepared and issued by CSI relating to the Cliquet Product.

2.4 The Cliquet Product was designed to provide capital protection and a guaranteed minimum return with the potential for more if the FTSE 100 Index performed consistently well. The potential for more was subject to a cap on the potential maximum return offered by the product. During the Relevant Period the maximum return figure given in the financial promotions varied between 20% and 72% for the 4 to 6 year versions of the Cliquet Product distributed by YBS. The guaranteed minimum return varied between 4% and 23.5% for the 4 to 6 year versions. Throughout the Relevant Period, YBS knew that there was close to a 0% probability of achieving the maximum return and a 40% to 50% chance of a

[1] The Cliquet Product is a 4, 5 or 6 year capital protected structured product, which guaranteed a minimum return and had a cap on the potential maximum earnings. The Cliquet Product generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100 (known as a 'cliquet' structure). The total return was calculated by taking the sum of the returns from each 6 month period throughout the lifetime of the product (subject to the minimum guaranteed return and a cap on the potential maximum return for each of the 6 month periods). For the maximum return to be achieved the FTSE 100 was required to steadily rise throughout the lifetime of the product.

customer only receiving the guaranteed minimum. Of the Cliquet Products that matured during the Relevant Period, (which had opened between 2003 and 2008 and were held through the financial crisis), across all distributors, 41% achieved more than the guaranteed minimum return. The remaining 59% of products achieved only the minimum. Overall, the average return above the guaranteed minimum was 2.57% (equating to an annual return of 0.45%) higher than the guaranteed minimum return. None of the issues of the Cliquet Product ever achieved the maximum return.

2.5 The Product Brochures (throughout the Relevant Period) and the majority of the YBS Financial Promotions (up until 24 September 2010) gave undue prominence to the potential maximum return. They cited the potential maximum return figure as one of the key promotional features of the Cliquet Product notwithstanding that, as YBS was aware, it was almost impossible to achieve the maximum return. While it was necessary to refer to the cap on returns in the financial promotions, given YBS's knowledge of the low likelihood of receiving the maximum return, it was highly inappropriate to emphasise the maximum return in this way.

2.6 This led to an unfair presentation of the likelihood of achieving the maximum return (and consequently the overall likely return). Customer surveys showed that the end result was a significant disparity between customer expectation and the actual likely returns (as set out in paragraph 2.4 above). A survey carried out by YBS in October and November 2010 found that around 18% of customers expected to achieve the maximum return compared to about 8% of whom expected to receive the minimum.

2.7 YBS relied on potential investors to infer the low likelihood of achieving the maximum return from the limited (and, in some cases, non-existent) explanations contained in the YBS Financial Promotions and the Product Brochures. In order to understand the likelihood of achieving anything above the minimum return, the Cliquet Product's potential customers required a high level of sophistication and experience. Given the profile of the Cliquet Product's customers, there was a significant risk that they would not possess sufficient understanding of structured products to fully understand the Cliquet Product from the content of the Product Brochures and the YBS Financial Promotions.

2.8 The Authority recognises that, as a result of concerns raised by third parties including the Authority, customers and Which?, changes were made to the YBS

Financial Promotions as a result of which, by 24 September 2010, undue prominence was no longer given to the potential maximum return in the YBS Financial Promotions. The effect of this change was a marked improvement in the overall presentational balance of the YBS Financial Promotions. Nevertheless, the YBS Financial Promotions (which continued to refer to the maximum return, albeit without giving it undue prominence) continued to give an unfair impression of the likelihood of achieving the maximum return for the reasons set out in paragraph 2.7 above.

2.9 The explanations of how returns on the Cliquet Product were calculated contained within the posters and certain flyers produced by YBS were unclear and gave rise to the risk that typical investors in the Cliquet Product would confuse the cliquet structure (which generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100) with a simple index tracker (which generated returns based on the overall growth of the FTSE 100 over the lifetime of the product). Although the typical investors in the Cliquet Product might have been able to assess the likelihood of any promoted rate of return on a simple index tracker, it would have been much more difficult for them to assess the likely rate of return on the Cliquet Product.

2.10 Until 18 January 2012, the Product Brochures and General Terms and Conditions failed to provide a sufficiently clear, full and prominent explanation to customers of the basis for the calculation of the level of charge that would apply to their investment in the event of early termination. Of the YBS customers who invested in the Cliquet Product during the Relevant Period, around 4% (2,088 customers) chose to withdraw from the product early. Of the customers who withdrew, approximately 15% (318 customers) had to pay an early exit fee. This was applied to the initial investment sum and, therefore, these customers received less than their initial investment back. The average early exit fee applied to customers who withdrew early was £269 (around 3% of the investment). The remaining approximately 85% (1,770 customers) who withdrew received their initial investment back without any accrued interest or return. Customers were unable to understand the basis for the calculation of the level of charge to be applied to the amount invested.

2.11 As a result of these matters, YBS did not pay sufficient regard to the information needs of customers.

2.12 The Authority considers YBS's failings to be particularly serious because:

1) financial promotions are often the primary source of information for customers seeking to understand a particular product prior to making a decision whether to invest. It is therefore essential that firms producing such materials ensure that the content of their communication provides customers with a balanced impression of the product. Issues with the product may only become fully apparent some years into the investment and exiting the product is often difficult and expensive;

2) the Authority has consistently stressed in its publications the importance of firms taking appropriate steps to ensure that communications with customers are clear, fair and not misleading;

3) the typical investors in the Cliquet Product were unsophisticated investors with limited investment experience and knowledge;

4) of the widespread availability of and investment in the Cliquet Product. YBS was the largest distributor of the Cliquet Product, responsible for approximately 75% of the total amount invested in the Cliquet Product. During the Relevant Period over 56,000 customers invested a total of approximately £545m in the 44 issues of the Cliquet Product distributed by YBS;

5) the changes made by YBS in September 2010 to reduce the prominence of the maximum return in its financial promotions were made at the instigation of third parties, including the Authority and Which?, rather than on YBS's own initiative;

6) the results of the consumer research commissioned by YBS during the Relevant Period, indicated that there was a significant disparity between customer understanding of the realistic potential returns from the Cliquet Product and the actual likely returns; and

7) the Cliquet Product was designed to be sold on a non-advised basis.

2.13 Following intervention from the Authority in June 2012, a number of material improvements were made to the Product Brochures and a customer contact exercise took place involving approximately 2,800 YBS customers who had agreed to enter into the latest tranches of the Cliquet Product (which had yet to close). These customers were provided with additional information on the likelihood of achieving returns from the product and offered the opportunity to withdraw their funds without incurring a penalty. Of those YBS customers who responded to the customer contact exercise, 17.15% decided to withdraw from the Cliquet Product (including some who withdrew for reasons other than new information). The remaining 82.85% confirmed that they wished to retain their investment. CSI and YBS have now agreed to extend this customer contact exercise. Customers who have queries on this exercise or who wish to make a complaint should contact CSI on 0800 052 0044 or visit www.ybs.co.uk.

2.14 The Authority acknowledges that YBS cancelled its distribution agreement with CSI in December 2012 and has suspended its sales of the Cliquet Product and all other structured deposit products pending the outcome of the Authority's investigation.

2.15 The Authority also acknowledges that during the Relevant Period, YBS considered that the absence of a significant level of customer complaints suggested consumers found the YBS Financial Promotions and the Product Brochures to be clear, fair and not misleading.

3. DEFINITIONS

3.1. The definitions below are used in this Final Notice:

"the Act" means the Financial Services and Markets Act 2000;

"AER" means Annual Equivalent Rate;

"the Authority" means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority;

"BBS" means Barnsley Building Society, a trading name of Yorkshire Building Society;

"BCOBS" means the part of the Authority's Handbook titled the Banking Conduct of Business Sourcebook;

"CBS" means Chelsea Building Society, a trading name of Yorkshire Building Society;

"Cliquet Product" means the capital protected structured cliquet product with a term of four, five or six years, which guaranteed a minimum return and had a cap on the potential maximum earnings, which was issued by CSI and sold on a non-advised basis through third-party distributors, including YBS, during the Relevant Period. The Cliquet Product distributed by YBS was originally known as the tracked growth version of the GIA but, from 6 April 2010, it was known as the tracked growth version of the PCA[2];

"COBS" means the part of the Authority's Handbook titled the Conduct of Business Sourcebook;

"CSI" means Credit Suisse International;

"Customer Contact Letter" means the letter sent to approximately 2,800 YBS customers from the latest tranches of the Cliquet Product (which had yet to close) in July 2012 providing them with additional information and giving them the opportunity to withdraw from these without incurring a charge;

"DEPP" means the Authority's Decision Procedure & Penalties Manual as set out in the Authority's Handbook;

"distributors" means YBS and other third party building society distributors;

"General Terms and Conditions" means the terms and conditions document which was normally distributed to customers at the same time as the Product Brochures (but was also available on YBS's web pages);

"GIA" means Guaranteed Investment Account. During the Relevant Period, YBS distributed 4 issues of the Cliquet Product in 2 tranches under the name "GIA".

"the Index" means the FTSE 100 Index;

"the Principles" means the Authority's Principles for Businesses as set out in the Authority's Handbook;

"PCA" means Protected Capital Account. During the Relevant Period, YBS distributed 40 issues of the Cliquet Product in 14 tranches under the name "PCA";

"Product Brochures" means the brochures prepared by CSI and approved by YBS as a financial promotion for the Cliquet Product and entitled "Plan Specific Terms and Conditions". Typically, these would have been provided to YBS's customers

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[2] It is noted that during the Relevant Period, in addition to the Cliquet Product, YBS distributed other products manufactured and issued by CSI (including fixed income, annual income and inflation linked products) which bore the names 'GIA' and 'PCA.' These products did not have a cliquet structure. The Authority did not consider the financial promotions relating to these as part of its investigation.

following an in-branch one to one meeting with a trained sales representative (but were also available on YBS's web pages);

"the Relevant Period" means the period between 1 November 2009 and 17 June 2012;

"the Rules" means the rules set out in the Authority's Handbook;

"the Tribunal" means the Upper Tribunal (Tax and Chancery Chamber);

"YBS" means Yorkshire Building Society. All references to YBS should be construed as including the Yorkshire, BBS and CBS trading names;

"YBS Financial Promotions" means the promotional flyers, branch posters, direct mail letters and web pages produced by YBS relating to the Cliquet Product during the Relevant Period; and

"Yorkshire" refers to YBS' "Yorkshire Building Society" trading name and branding, as distinct from the BBS and/or CBS trading names.

4. FACTS AND MATTERS

BACKGROUND

Yorkshire Building Society

4.1 YBS is the UK's second largest building society with over 3.5 million members. YBS has been authorised by the Authority since 1 December 2001.

4.2 Throughout the Relevant Period, YBS distributed the Cliquet Product through its Yorkshire Building Society and Barnsley Building Society brands. On 1 April 2010, YBS merged with Chelsea Building Society. Following the merger, YBS also distributed the Cliquet Product through its CBS brand. Throughout the Relevant Period the branding, font colour and sizes, and therefore the 'look and feel' of the Yorkshire, BBS and CBS financial promotions differed.

4.3 Despite the different brandings used, the contents of the Yorkshire, BBS and CBS financial promotions were broadly similar for the majority of the Relevant Period. Where differences were present that are relevant to the Authority's findings, these are set out in paragraphs 4.21 to 4.38 and 4.45 to 4.50 below.

The Cliquet Product

4.4 During the Relevant Period, YBS launched and distributed 44 issues of the Cliquet Product, into which 56,236 investors invested a total amount of approximately £545 million in deposits. The average amount invested by YBS's customers in each Cliquet Product during the Relevant Period was approximately £9,700.

4.5 The Cliquet Product is a capital protected structured product with a term of four, five or six years, which guaranteed a minimum return and had a cap on the potential maximum earnings. The Cliquet Product was sold by YBS in tranches. At any one time, there may have been a number of consecutive issues in distribution within a tranche with different four to six year investment terms. The different issues of each of these would be numbered and, therefore, for example, the first issue of the PCA would be described as "PCA 1".

4.6 The Cliquet Product was designed to be suitable for the '*stepping stone customer*.' '*Stepping stone customers*' were typically conservative, risk averse customers with at least £3,000 available to invest for a fixed period of 4 to 6 years. These investors typically sought more competitive returns than those offered by deposit accounts but were unwilling to take a large step away from fixed rate investments. Retail investors who entered into the Cliquet Product were typically unsophisticated investors with limited investment experience and knowledge. Across all distributors, the age profile of the investors was 14.5% under 45%, 53% between 45 and 65 and 32.5% over 65.

4.7 The Cliquet Product was developed to be fundamentally similar in nature to other deposit products typically offered to '*stepping stone customers*' by building societies. The Cliquet Product offered capital protection and a guaranteed minimum return with the potential for some higher growth if the Index consistently increased during the life of the Cliquet Product. On this basis, YBS assessed the Cliquet Product as being low-risk, non-complex and suitable for non-advised sales to retail customers. During the Relevant Period, YBS mostly sold the Cliquet Product to customers following an in-branch one to one meeting between the customer and a trained sales representative where the Cliquet Product (and potentially other products) was explained. The sale itself was conducted on a non-advised basis.

4.8 The Cliquet Product was designed primarily to provide capital protection and a guaranteed minimum return. The by-product of providing this guaranteed return was the introduction of a cap or limit on the potential maximum return.

4.9 The YBS Financial Promotions and Product Brochures provided by YBS to its customers highlighted potential maximum returns, which varied between 20% and 72% for the 4 to 6 year versions of the Cliquet Product, and guaranteed minimum returns, which varied between 4% and 23.5%, during the Relevant Period. The Product Brochures (throughout the Relevant Period) and the majority of the YBS Financial Promotions (up until September 2010) gave equal, or near equal, prominence to the minimum return and maximum return (see paragraphs 4.21 to 4.44 below). The Cliquet Product generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100 (known as a 'cliquet' structure). Any positive returns secured during any of the six month periods would be offset by any negative returns in other six month periods. The total return was calculated by taking the sum of returns from each six month period throughout the lifetime of the product (subject to the minimum guaranteed return and a cap on the potential maximum return for each of the 6 month periods). For the maximum return to be achieved the FTSE 100 was required to steadily rise throughout the lifetime of the product.

4.10 Throughout the Relevant Period, YBS was aware that the likelihood of achieving the maximum return was close to 0%. Further, analysis carried out by Which? and CSI and shared contemporaneously with YBS, showed that the conditions required to achieve the advertised headline rates had not occurred since the start of the period analysed (1984, which was when the FTSE 100 was launched). Analysis shared with YBS also showed that there was an approximately 40% to 50% chance of a customer only achieving the minimum return. 82 Cliquet Products matured during the Relevant Period (all of which had been opened between 2003 and 2008) and 59% of the maturing Cliquet Products paid out only the guaranteed minimum return whilst none of the remaining 41% delivered the maximum return. Overall, the average return above the guaranteed minimum was only 2.57% (equating to an annual return of 0.45% higher than the guaranteed minimum return). None of the issues of the Cliquet Product ever achieved the maximum return.

The financial promotions

4.11 Throughout the Relevant Period, YBS prepared and issued the YBS Financial Promotions. These included:

1) <u>Direct Mail Letters</u> which were posted to customers who met the product profile and typically comprised a letter addressed to the customer together

with leaflets seeking to explain how the product worked;

2) Branch Posters which appeared in the external windows of branches and would therefore typically have been seen by customers walking past a branch;

3) Promotional Flyers which were placed in leaflet dispensers within branches, and would therefore typically have been encountered by a customer when visiting a branch; and

4) Web Pages on YBS's website, which could be accessed either independently by the customer or using an emailed link sent to them by YBS.

4.12 Of the four categories of YBS Financial Promotions listed above, not all categories of financial promotion were generated for each issue, or even for each tranche of the Cliquet Product.

4.13 Customers could not directly invest in the Cliquet Product as a result of seeing or receiving the YBS Financial Promotions and would typically visit a branch (or, in the case of customers who viewed the web pages, return a signed application form by post) in order to invest in the Cliquet Product.

4.14 Throughout the Relevant Period, YBS also provided its customers with Product Brochures prepared by CSI, and reviewed and approved by YBS. The Product Brochures were the primary source of written information for customers seeking to understand the product prior to making the decision whether to invest. Typically, the Product Brochures would be provided by YBS to its customers as part of its sales process.

4.15 The accuracy and clarity of the YBS Financial Promotions and the Product Brochures were particularly important because the:

1) investors in the Cliquet Product comprised '*stepping stone customers*' who were typically unsophisticated investors with limited or no experience of complex structured deposit products, such as the Cliquet Product;

2) Cliquet Product was developed with the expectation that it would be sold on a non-advised basis; and

3) terms and conditions for the Cliquet Product included an early exit fee which could vary significantly depending on the circumstances.

Prominence of, and likelihood of achieving, the maximum return

4.16 The Product Brochures (throughout the Relevant Period) and the majority of the YBS Financial Promotions (up until 24 September 2010) gave undue prominence to the potential maximum return. They cited the potential maximum return figure as one of the key promotional features of the Cliquet Product notwithstanding that, as YBS was aware, it was almost impossible to achieve the maximum return.

4.17 Although the Product Brochures and most of the YBS Financial Promotions contained explanations of the likelihood of achieving the maximum return, these were not adequate for the target market for which these products were intended as they created an unfair impression as to the achievability of that return. This impression was evident from customers' expectations of returns: in a customer survey of 300 YBS customers conducted in October and November 2010, 18% of customers surveyed (all of whom had at least received a Product Brochure) expected to achieve the maximum return despite the fact this was almost impossible to achieve. The unfair impression was exacerbated in the YBS posters (throughout the Relevant Period) and the CBS flyers (between 6 April 2010 and 1 August 2010), as these did not contain any explanation at all of the conditions necessary to achieve the maximum return.

4.18 As set out above, YBS was aware that the likelihood of achieving the maximum return was extremely remote (i.e. close to 0%). YBS sought to set out the conditions required to obtain the maximum return, which did not refer to the results of analysis shared with it, and relied on potential investors to infer the low likelihood of achieving the maximum return from the limited (and in the case of the YBS posters and the early versions of the CBS Flyers, non-existent) explanations contained in the YBS Financial Promotions and the Product Brochures. These explanations required a high level of sophistication from potential investors which, given the intended target market, there was a significant risk those customers would not possess. This meant the content of the YBS Financial Promotions and the Product Brochures did not pay sufficient regard to the information needs of customers.

4.19 From August 2010, back testing results were discussed between YBS and CSI on a regular basis as part of face to face discussions relating to the Cliquet Product. In November 2011, CSI developed a Structured Product Evaluation Pack to provide additional guidance to distributors (including YBS) about the Cliquet

Product features and the applicable target market. This pack included information regarding historical performances and expected probabilities, market commentary, and an analysis of the target market. As this document was directed at distributors, it carried the warning: *"This material is solely directed at Professional Clients and Eligible Counterparties as defined by the FSA, and is not directed at, and should not be relied upon by, Retail Clients."* The Structured Product Evaluation Pack included the following explanation regarding the maximum return:

"As would be expected, the model driven probabilities suggest approximately a 50% chance of receiving only the minimum return (when the market falls or is flat), and a strong possibility of achieving AERs above this (up to around 4.5% AER, or 5% to 6% AER for longer maturities), and then a limited and decreasing possibility at higher levels."

"The back testing does not reveal instances of all periods hitting the Cap % to produce the highest level of return. This is consistent with the low probability recorded for this occurrence, and should be noted in the product documents."

4.20 In fact, the only reference to the low probability of hitting the cap % in the "product documents" was the wording at paragraphs 4.23, 4.32, 4.36 – 4.37 and 4.41 – 4.43 below.

Direct Mail Letters

4.21 At the beginning of the Relevant Period in November 2009, the Yorkshire direct mail letters included both the guaranteed minimum return and the potential maximum return with equal or close to equal prominence. During this period, the maximum returns were given significant prominence on the front page of the direct mail letters, appearing in distinctive colour bubbles and in bold large fonts.

4.22 The font size of the maximum return within the Yorkshire direct mail letters was reduced from PCA 5, launched on 28 May 2010 onwards, in response to a customer complaint. From this point onwards, the maximum return was approximately half the size of the font used to display the minimum return in the Yorkshire direct mail letters. Nevertheless, significant prominence continued to be given to the maximum return within the Yorkshire direct mail letters up until the tranche launched on 24 September 2010.

4.23 At the beginning of the Relevant Period, the Yorkshire direct mail letters sought to explain the low likelihood of achieving the maximum return using the following wording:

"To earn [the maximum return of] XX%, the growth in each of the X periods would need to be plus X%..."

4.24 Although different wording was used in the early versions of the CBS direct mail letters, the substance was almost identical. No direct mail letters were produced by BBS during the Relevant Period.

4.25 The wording used to explain the low likelihood of achieving the maximum return remained fairly constant throughout the Relevant Period. Although changes were made to the wording from PCA 17, launched on 4 January 2011, these changes did not materially alter the explanation of the low likelihood of achieving the maximum return, nor, for the reasons set out in paragraph 4.18 above, were these explanations adequate for the target market.

Posters

4.26 At the beginning of the Relevant Period in November 2009, the posters gave significant prominence to both the guaranteed minimum and the potential maximum return, with the return figures appearing in distinctive colours, in bold fonts and in significantly larger font sizes than anything else on the page. Although the maximum return was displayed in a smaller font size compared to the minimum return within the posters, it nevertheless featured very prominently. Significant prominence continued to be given to the maximum return within the posters up until the tranche launched on 24 September 2010.

4.27 The posters did not contain any explanation at all of the conditions necessary to achieve the maximum return.

4.28 By way of example, the following is an extract from the Yorkshire poster for the Guaranteed Investment Account – TG 6, which opened on 6 November 2009:

Flyers

4.29 At the beginning of the Relevant Period in November 2009, the flyers gave significant prominence to both the guaranteed minimum and the potential maximum returns, with the return figures appearing in distinctive colours, in bold fonts and in significantly larger font sizes than anything else on the page. Although the maximum return was displayed in a slightly smaller font size compared to the minimum return, it nevertheless featured very prominently on the front page of the flyers.

4.30 By way of example, the following is an extract from the front page of the Yorkshire flyer for the Guaranteed Investment Account – TG 5, which opened on 6 November 2009:

4.31 Significant prominence continued to be given to the maximum return within the flyers up until the tranche launched on 24 September 2010.

4.32 At the beginning of the Relevant Period, the Yorkshire and BBS flyers sought to explain the low likelihood of achieving the maximum return using the following wording:

"To achieve [the maximum return of] XX% growth, the reading would have to be at least +X% in every 6-monthly period in the investment term."

4.33 In contrast, the CBS flyers issued between 6 April 2010 and 1 August 2010 did not contain any explanation of the likelihood of the maximum return being achieved. Beyond this date, the wording used in the CBS flyers to explain the likelihood of the maximum return being achieved was identical to that used in the Yorkshire and BBS flyers.

4.34 The wording used to explain the low likelihood of achieving the maximum return remained broadly constant throughout the Relevant Period. Although changes were made to the wording from PCA 9, launched on 24 September 2010, these changes did not materially alter the explanation of the low likelihood of achieving the maximum return, nor, for the reasons set out in paragraph 4.18 above, were these explanations adequate for the target market.

<u>Web Pages</u>

4.35 At the beginning of the Relevant Period in November 2009, the Yorkshire web pages contained a web banner which gave significant prominence to both the guaranteed minimum and the potential maximum return, with the return figures appearing in distinctive colours and in bold, large fonts, with equal or close to equal prominence. Significant prominence continued to be given to the potential maximum return within the Yorkshire web pages up until PCA 4, which formed part of a tranche launched on 28 May 2010.

4.36 At the beginning of the Relevant Period, the web pages sought to explain the low likelihood of achieving the maximum return using the following wording:

"To earn [the maximum return of] XX% growth, the change would need to be +X% in each of the periods…"

4.37 From PCA 4, launched on 28 May 2010, this wording was amended so that it now read as follows:

"For example, to earn [the maximum return of] *XX% growth with Tracked Growth X, the FTSE 100 would have to rise by at least +X% in each of its X six monthly*

periods during the term…"

4.38 No further amendments were made to this wording during the Relevant Period. For the reasons set out in paragraph 4.18 above, both the explanations provided were inadequate for the target market.

<u>Product Brochures</u>

4.39 At the beginning of the Relevant Period in November 2009, the Product Brochures included both the guaranteed minimum and potential maximum return with equal, or close to equal, prominence.

1) By way of example, the front page of the Product Brochure for the Guaranteed Investment Account – TG 5, which opened on 6 November 2009, included the following information:

2) Page 3 of the Product Brochure for the Guaranteed Investment Account - TG 5 stated the following:

> **How does the Plan work?** You will receive your capital back on the Plan Maturity Date and:
>
> 11.25% minimum growth
>
> or up to a maximum of 50% growth
>
> dependent upon the performance of the FTSE® 100 Index as outlined below

4.40 During the Relevant Period, two additional changes were made to the Product Brochures the effect of which was to exacerbate the unfair presentation of the possibility of achieving the maximum return (and consequently the overall likely return). These were carried over into subsequent launches of the Cliquet Product over the Relevant Period. These amendments were:

1) the introduction of a table setting out examples of possible gross returns on £10,000 provided that the Cliquet Product is held until the maturity date. Four scenarios were included with equal prominence given to the guaranteed minimum and the potential maximum return. The examples section was first introduced for the PCA 1 tranche in April 2010 and this element was included in the financial promotions for 40 of the YBS Cliquet Product launches;

2) the reduction of the size of the font used for the prominent minimum growth figure on page 3 of the Product Brochures, with the impact of matching it with that used for the 'maximum' growth figure. In the Product Brochures for the Cliquet Product issues that opened up to 18 January 2012, the font sizes had been chosen to maintain a small distinction between the two figures in the second reference to the minimum and maximum return on page 3 of the Product Brochures, with the aim of giving the guaranteed minimum return some additional prominence over that of the potential maximum return figure. In later issues, the Product Brochures gave the guaranteed minimum return and maximum return equal prominence (in terms of font size and presentation).

4.41 The Product Brochures sought to explain the low likelihood of achieving the maximum return with the following wording (which appeared twice):

"The maximum growth of XX% will only be achieved if the percentage gain in the Index if X% or more for each of the consecutive semi-annual periods."

4.42 From the launch of PCA 4 opening on 28 May 2010, this wording was slightly amended to include the words *"and every one".* This change was intended to add extra emphasis in the Product Brochures to the conditions which needed to be met in order to achieve the maximum return. After this addition the new explanatory text read as follows:

"*The maximum growth of XX% will only be achieved if the percentage gain in the Index is X% or more for each and every one of the consecutive semi-annual periods".*

4.43 A positive change was also implemented into the relevant text in the Product Brochures. However, this was included after Which? approached CSI and YBS in September 2010 with concerns about the Cliquet Product and the completion of a customer survey rather than as a result of YBS identifying pro-actively the need to alter the Product Brochures. The change was to underline the text set out in paragraph 4.42 above, seeking to explain the circumstances in which the maximum return would be achieved. The effect of this was to place some additional emphasis on the terms that needed to be met to achieve the maximum return.

"*The maximum growth of XX% will only be achieved if the percentage gain in the Index is X% or more <u>for each and every one of the consecutive semi-annual periods."</u>*

4.44 This amendment was implemented for the PCA 12 launch that opened on 12 November 2010. The change affected the Product Brochures for 29 issues of the Cliquet Product distributed by YBS. The change increased the emphasis on the relevant phrase but provided no further explanation. Notwithstanding this positive change, for the reasons set out in paragraph 4.18 above, the explanations provided remained inadequate for the target market.

Basis for calculation of returns

4.45 As set out above, the cliquet structure generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100.

4.46 The posters produced by YBS (for all brands, and throughout the Relevant Period) and the CBS flyers (between 6 April 2010 and 1 August 2010) contained an unclear explanation of how the returns on the Cliquet Product were calculated.

4.47 At the beginning of the Relevant Period, the only explanation contained in the Yorkshire and BBS posters of how returns on the Cliquet Product were calculated was:

"…with potential maximum growth of XX% gross based on potential FTSE 100 index growth during the full X-year term."

4.48 Similar wording was also used in early versions of the CBS posters and flyers.

4.49 Changes were made to the wording contained in the posters from PCA 11 onwards, which formed part of a tranche launched in September 2010. Beyond this date, the explanation of how returns on the Cliquet Product were calculated read as follows:

"The return… could be up to XX% gross (X% AER) as it is based on the performance of the FTSE 100 index without actually being invested in the stock market."

4.50 Notwithstanding this change, the explanations of how returns on the Cliquet Product were calculated contained within the posters and the early versions of the CBS flyers were unclear and gave rise to the risk that customers would confuse the cliquet structure (which, as described in further detail in paragraph 4.9 above, generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100) with a simple index tracker (which generated returns based on the overall growth of the FTSE 100 over each of the 6 month periods in question). This difference was significant because although typical investors in the Cliquet Product might have been able to assess the likelihood of any promoted rate of return on a simple index tracker, it would have been much more difficult for them to assess the likely rate of return on the Cliquet Product (which was subject to the volatility of the FTSE 100 Index over each of the 6 month periods in question). Accordingly, there was a risk that customers may have wrongly assumed that the chances of achieving the maximum return were in fact greater than they actually were.

Explanation of the early exit fee

4.51 Of the YBS customers who invested in the Cliquet Product during the Relevant Period, as at September 2013, 2,088 customers had terminated investments involving the Cliquet Product early (approximately 4% of all YBS PCA customers). Where a customer terminated early, the Cliquet Product terms and conditions provided for the application of the early exit fee.

4.52 There were a number of factors which needed to be taken into account to calculate the early exit fee (see paragraph 4.61 below). This made it impractical to quantify it for each customer in advance. The average investment in the product by YBS customers during the Relevant Period was approximately £9,700. As at September 2013, almost 4% of those who had invested in the Cliquet Product during the Relevant Period had chosen to withdraw from the product early. Of the approximately 4% of customers who withdrew from the Cliquet Product around 15% (318 customers) had to pay an early exit fee. This was applied to the initial investment sum and, therefore, these customers received less than their initial investment back. The average early exit fee applied to customers who withdrew early was £269 (around 3% of the investment). The remaining approximately 85% (1,770 customers) who withdrew received their initial investment back without any accrued interest or return.

4.53 The only reference in the Product Brochures to the early exit fee to be applied in the event of early termination was:

"You will have 14 days from the date of receipt of details of your cancellation rights to change your mind and cancel your investment.

Following the 14 day period any early encashment will result in an early exit fee (including in the event of death) and so you will get back less than you initially invested.

Please see the General Terms & Conditions for details relating to your cancellation rights (clause 5) and early encashment (clause 6)."

4.54 On page 2 of the Product Brochures, throughout the Relevant Period, there was an additional warning to customers:

"*Please note that the Plan is intended to be held until the Plan Maturity Date. You should have enough emergency funds elsewhere as the Plan is not designed for early encashment."*

4.55 The wording in paragraphs 4.53 and 4.54 above was slightly amended in the period up to January 2012 with the intention of adding extra emphasis to the early exit fee in the Product Brochures. However, these changes did not materially alter the explanation of the early exit fee given by the Product Brochures.

4.56 The General Terms and Conditions read as follows:

"If you cash in your investment or transfer your Account after the 14-day cancellation period … but before the Plan Maturity Date (including in the event of death), an Early Termination Amount will be paid to you. The Early Termination Amount will be your Initial Investment less an Early Exit Fee and so you will get back less than you originally invested. Any Early Termination Amount will not include any other amounts which would otherwise be payable if the Account were held until the Plan Maturity Date.

'Early Exit Fee' means an amount calculated by the Deposit Taker by reference to the amount initially deposited by you and is determined at the relevant time based on prevailing market conditions such as, but not limited to, interest rates and the level of any relevant Index."

4.57 The Cliquet Product was intended to be held until the end of the investment term. This was communicated to customers through different statements throughout the Product Brochures. From November 2009 until April 2010, the statement on the front cover of the Product Brochures stated that:

"100% Capital Guaranteed provided that the Account is held for the full Investment Term."

4.58 From April 2010 until the end of the Relevant Period, the front cover statement read as follows:

"Potential return dependent on the FTSE 100 Index … PLUS your Initial Investment back at maturity provided that the Account is held for the investment term."

4.59 Until November 2010, early termination of the Cliquet Product resulted in an early exit fee, including in the event of death. From the launch of PCA 12 on 12 November 2010 onwards, the early exit fee no longer applied in the event of death.

4.60 The Product Brochures and General Terms and Conditions issued prior to January 2012 contained explanations of the effect of the early exit fee that were not sufficiently clear, full and prominent. The Authority recognises that it was not possible to quantify the early exit fee for each customer in advance. However, CSI and YBS should have provided sufficient information to customers to allow them to understand the basis on which the fee would be calculated.

4.61 From the launch of PCA 36 on 18 January 2012, a section entitled *'What should I expect from the Early Exit Fee?'* was added to the Product Brochures to explain to customers the factors that would be taken into account when the early exit fee was calculated. This stated:

"If you exit your investment before the Plan Maturity Date, and the value of your investment at the time of exit is lower than your Initial Investment, an Early Exit Fee will be charged which is equivalent to the shortfall in value of your Initial Investment. A number of factors have significant bearing on the calculation of any Early Exit Fee.

- *The presence of up front commissions or charges incurred at Issue Date, as set out in Clauses 11 and 13 of the General Terms and Conditions, will increase the size of the Early Exit Fee.*

- *The higher the minimum return for the Plan and the closer the Plan is to maturity, the lower the Early Exit Fee will be.*

- *The Early Exit Fee will also be linked to interest rates used by banks when lending to each other at the time of exiting the Plan. For example, after Issue Date, should interest rates (for the life of the Plan) rise, any Early Exit Fee is likely to increase in size.*

- *The observed, up to point of exit, and expected performances of the Index up to the Plan Maturity Date will affect the Early Exit Fee. Positive performances of the Index may reduce, whilst negative may increase, any potential Early Exit Fee.*

- *Other market factors could impact the calculation of the Early Exit Fee, such as, but not limited to: the cost to the Deposit Taker of replacing the monies returned early, or how volatile the Index is."*

4.62 This element was included in the Product Brochures for 5 issues of the Cliquet Product distributed by YBS. By setting out these factors in the product literature, sufficient improvements were made to avoid making the Product Brochures unfair from 18 January 2012 onwards. In addition, text explaining that partial withdrawals were not permitted was included for the PCA 39 launch which opened on 6 April 2012. This change affected the Product Brochures for 2 issues of the Cliquet Product distributed by YBS.

Improvements made to prominence of maximum return in 2010

4.63 In September 2010, Which? wrote to YBS expressing a number of concerns relating to the Cliquet Product. Some of these were similar to concerns conveyed to YBS by the Authority in March 2010 about the excessive prominence given to the potential maximum return in YBS's promotional materials despite the remote likelihood of the attainability of that return. Prompted by the concerns raised by Which?, from the launch of PCA 9 which opened on 24 September 2010, YBS amended the layouts of the direct mail letters, posters and flyers, as a result of which the maximum return was no longer given undue prominence in the YBS Financial Promotions. As noted in paragraph 4.35 above, changes had already been made to the prominence of the maximum return in the web pages in advance of this date.

4.64 The effect of this change was a marked improvement in the overall presentational balance of the YBS Financial Promotions. The only return given significant prominence in the YBS Financial Promotions from this point onwards was the minimum return. These changes affected a total of 32 issues of the PCA.

4.65 Notwithstanding the improvements made to the YBS Financial Promotions in September 2010, the YBS Financial Promotions continued to give an unfair presentation of the likelihood of achieving the maximum return for the reasons set out in paragraph 4.18 above. In addition, for the reasons set out in paragraphs 4.45 – 4.50 above, the posters produced by YBS beyond this date continued to contain an inadequate explanation of how returns on the Cliquet Product were calculated to enable YBS's target market of '*stepping stone customers*' to distinguish it from a simple index tracker.

4.66 Despite making improvements to the YBS Financial Promotions during 2010 to reduce the prominence of the minimum return, YBS did not take steps to ensure that the prominence of the potential maximum return was similarly reduced in the Product Brochures.

Customer experience survey

4.67 YBS commissioned a customer experience survey in October and November 2010 involving 300 customers as a means of assessing the validity of Which?'s concerns. The results of this survey found that around 18% of customers expected to achieve the maximum growth compared to about 8% who expected to receive the minimum return at the end of the investment term. The remaining 73% expected to receive growth somewhere between the minimum and maximum returns (with no further details of the exact level expected being requested).

4.68 The high proportion of Cliquet Product customers expecting to achieve the maximum return was also demonstrated by subsequent customer surveys carried out by YBS. Between March 2011 and July 2012, YBS conducted a further 9 customer experience surveys, which involved contacting customers who had purchased the Cliquet Product during the Relevant Period. The results of these surveys revealed that the number of customers expecting to attain the maximum return in full varied between 13% and 25%.

4.69 YBS was aware that there was a close to a 0% probability of achieving the maximum return and a 40% to 50% chance of a customer only receiving the minimum return. During the Relevant Period, across all distributors, 41% of maturing Cliquet Products (which opened between 2003 and 2008) achieved more than the guaranteed minimum return. The remaining 59% of products achieved only the minimum. Overall, the average additional return realised was only 2.57% (equating to an annual return of 0.45%) above the guaranteed minimum return. None of the Cliquet Products delivered the maximum return and, as YBS was aware, there was a close to 0% chance of this. If these statistics are compared with the results of the customer experience surveys it is apparent that there was a significant disparity between customer expectations and the actual likely returns. YBS should have taken steps to improve the YBS Financial Promotions and the Product Brochures to make them clear, fair and not misleading to the target market of '*stepping stone customers.*'

4.70 The customer experience surveys commissioned by YBS included full responses from customers. Some of these customer responses demonstrated a lack of understanding on the part of those customers of how the cliquet structure worked and how returns at the end of the investment term were calculated. This highlighted the target market's limited investment knowledge and experience. The results of these customer experience surveys should have prompted YBS to challenge whether the content of the financial promotions satisfied the clear, fair and not misleading criteria and whether the YBS Financial Promotions and the Product Brochures contained a balanced presentation of the potential returns available. However, YBS did not review or make any amendments to the financial promotions as a result of these surveys.

Customer contact exercise

4.71 Following intervention from the Authority in June 2012, approximately 2,800 YBS customers who had agreed to enter into the latest tranches of the Cliquet Product (which had yet to close) were each sent a Customer Contact Letter. The purpose of the Customer Contact Letter was to rectify the breaches in the Product Brochures and to allow consumers to make a fully informed choice regarding their original decision to invest in the Cliquet Product.

4.72 The wording of the Customer Contact Letter stated that the Authority had *"expressed concern that [customers] may have been given the wrong impression as to the likelihood of receiving the maximum return for [the relevant issue of the Cliquet Product]", the* Customer Contact Letter also explained that CSI had:

1) *"calculated how [the relevant Cliquet Product] would have performed historically, looking at the growth returned on theoretical investments in the FTSE® 100 Index starting each day since its inception in 1984. The calculations [demonstrated] that:*

- *In just over half of the cases an investment in [the relevant Cliquet Product] would have delivered the minimum return.*

- *In the majority of remaining cases [the relevant Cliquet Product] would have returned an amount much closer to the minimum return than the maximum return.*

- *[The relevant Cliquet Product] would not have delivered a return of [maximum return]% ([maximum]% AER), which [was] the stated maximum."*

4.73 There was a 98% response rate to the letter. Of the YBS customers who responded 17.15% withdrew from the Cliquet Product after receiving the Customer Contact Letter. The remaining 82.85% chose to remain in the investment. Customers were also asked to tick a box explaining the reason for their withdrawal. Of those who responded 10.54% referred to the additional information specifically. In addition, 2.39% did not select a response, 0.62% ticked "Other", 1.95% stated that their financial situation had changed, 1.21% stated that the product no longer suited their needs and 0.44% now preferred an alternative product. Of these only the change in financial circumstances category was clearly unconnected to the additional information provided in the Customer Contact Letter.

5. FAILINGS

Breach of Principle 7 and related BCOBS Rules

5.1 In breach of Principle 7, YBS failed to pay due regard to the information needs of its clients by:

1) producing its own financial promotions, namely the YBS Financial Promotions, which did not satisfy the requirement to be clear, fair and not misleading; and

2) approving and providing to its customers Product Brochures for the Cliquet Product which did not satisfy the requirement to be clear, fair and not misleading.

5.2 In addition, considering YBS's breach of Principle 7, the Authority also finds that YBS breached certain of the detailed rules contained in the BCOBS part of the Authority's Handbook. The specific nature of YBS's breaches is set out in paragraphs 5.3 to 5.10 below.

Undue prominence of the potential maximum return

5.3 All 44 issues of the Product Brochures (throughout the Relevant Period); the Yorkshire web pages (up until 28 May 2010); the YBS flyers and posters (up until 24 September 2010); and the Yorkshire direct mail letters (up until 24 September 2010) gave undue prominence to the maximum return. This led to an unfair presentation of the likelihood of achieving the potential maximum return (and consequently the overall likely return).

5.4 The following factors contributed to the unfair prominence of the potential maximum return in both the YBS Financial Promotions and the Product Brochures:

1) the presentation of the 'potential maximum return' figure as one of the key promotional features in the Product Brochures (throughout the Relevant Period) and the majority of the YBS Financial Promotions (up until 24 September 2010) when it was only a by-product of the guaranteed minimum return and YBS knew that there was virtually no chance of the potential maximum return being achieved;

2) the substantially less prominent presentation of the explanation of the conditions necessary to achieve the potential maximum return than the reference to the maximum return itself in the Product Brochures (throughout the Relevant Period) and in the majority of the YBS Financial Promotions (up until 24 September 2010);

3) the unclear wording used in the Product Brochures and the YBS Financial Promotions (to the extent that an explanation was given at all) to explain the conditions necessary to achieve the potential maximum return;

4) the typical investors in the Cliquet Product were unsophisticated investors with limited investment experience and knowledge;

5) the Cliquet Product was sold on a non-advised basis; and

6) the results of the consumer research commissioned by YBS during the Relevant Period indicated that there was a significant disparity between customer understanding of the realistic returns from the Cliquet Product and the actual likely returns.

5.5 The following additional factors contributed to the unfair prominence of the potential maximum return in the YBS Financial Promotions:

1) the near equal prominence given to both the guaranteed minimum return and the potential maximum return, both of which appeared in distinctive colours, in bold fonts and in significantly larger font size than the surrounding text in the majority of the YBS Financial Promotions up until 24 September 2010; and

2) a failure to explain the conditions necessary to achieve the maximum return in the posters (throughout the Relevant Period) and the CBS flyers (between 6 April 2010 and 1 August 2010).

5.6 The following additional factors contributed to the unfair prominence of the potential maximum return in the Product Brochures:

1) the equal prominence given to both the guaranteed minimum return and the potential maximum return on the front page of the Product Brochures;

2) the presentation of the potential maximum return on the front page of the Product Brochures without qualifying the terms that needed to be met in order to attain that return until page 3 of the Product Brochures;

3) the prominent reference to the minimum return in a larger font size to that of the text around it, followed by a prominent reference to the potential maximum return (in slightly smaller font size to that used for the minimum return up to 18 January 2012 and exactly the same font size thereafter), and significantly larger than the surrounding text on page 3 of the Product Brochures; and

4) the table on page 4 of the Product Brochures setting out examples of possible gross returns on £10,000 with four scenarios including one representing the potential maximum return.

Breaches of related BCOBS Rules

5.7 The YBS Financial Promotions and the Product Brochures referred to (and, at least prior to September 2010, unduly emphasised) the potential maximum return without giving a fair and prominent indication of the remoteness of the potential to achieve the maximum return. YBS was aware that the probability of achieving the maximum return was close to 0% but did not make this clear in its financial promotions. During the Relevant Period, across all distributors, 41% of maturing products (which opened between 2005 and 2008) provided returns above the guaranteed minimum. Overall, the average returns were 2.57% (equating to an annual return of 0.45%) higher than the minimum guaranteed return.

5.8 The YBS Financial Promotions and the Product Brochures, therefore, contained information which was insufficient for the target '*stepping stone customers*' and unfairly emphasised the potential maximum return without giving a fair and prominent explanation of the likelihood of achieving the minimum return. Customers, as YBS knew or should have known as a result of the survey results, and other warnings, were unlikely to understand the remoteness of the possibility of achieving the maximum return, or anything above the minimum return, from the YBS Financial Promotions and the Product Brochures alone. This meant the content of the YBS Financial Promotions and the Product Brochures failed to pay due regard to the information needs of YBS's clients, failed to communicate information to customers in a way that was clear, fair and not misleading and prevented them from making decisions regarding the product on an informed basis. In this regard, YBS also breached BCOBS 2.3.1R and BCOBS 4.1.1R.

Basis for Calculation

5.9 The posters produced by YBS, throughout the Relevant Period, as well as the CBS flyers (between 6 April 2010 and 1 August 2010) failed adequately to explain how the returns on the Cliquet Product were calculated. The explanations contained in the posters and early versions of the CBS flyers were unclear and gave rise to the risk that customers would confuse the cliquet structure (which generated returns through a series of 6 month options over the lifetime of the product based on the growth of the FTSE 100) with a simple index tracker (which generated returns based on the overall growth of the FTSE 100 over the lifetime of the product). In this regard, YBS also breached Principle 7 and BCOBS 2.3.1R and BCOBS 4.1.1R.

Explanation of Early Exit Fee

5.10 Until 18 January 2012, the Product Brochures failed to provide a sufficiently clear, full and prominent explanation to customers of the level of charge that would apply to their investment in the event of early termination. Customers were unable to understand the basis for the calculation of the level of charge to be applied to the amount invested. In this regard, YBS also breached Principle 7 and BCOBS 2.3.1R and BCOBS 4.1.1R.

5.11 Annex A sets out extracts from statutory and regulatory provisions and guidance relevant to this Final Notice.

6. SANCTION

6.1 The Authority's policy for imposing a financial penalty is set out in Chapter 6 of DEPP.

6.2 Changes to DEPP were introduced on 6 March 2010. In respect of conduct occurring on or after 6 March 2010, the Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5A sets out the details of the five-step framework that applies in respect of financial penalties imposed on firms. In this case, as the Relevant Period is 1 November 2009 to 17 June 2012, the Authority has applied the five-step framework to calculate the appropriate penalty for YBS's breaches because the vast majority of the misconduct occurred within the period of the new penalty regime.

Step 1: disgorgement

6.3 Pursuant to DEPP 6.5A.1G, at Step 1 the Authority seeks to deprive a firm of the financial benefit derived directly from the breach where it is practicable to quantify this. Given the misconduct relates to the financial promotions for the Cliquet Product alone it is impracticable to identify the direct financial benefit YBS derived from it.

6.4 Further, as YBS has, in conjunction with CSI, agreed to carry out a customer contact exercise, any financial benefit will be negated.

6.5 Step 1 is therefore £0.

Step 2: the seriousness of the breach

6.6 Pursuant to DEPP 6.5A.2G, at Step 2 the Authority determines the figure that reflects the seriousness of the breach. Where the amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breach may cause, that figure will be based on a percentage of the firm's revenue from the relevant products or business area.

6.7 The Authority considers that the total revenue generated by YBS from the sale of all 44 issues of the Cliquet Product during the Relevant Period is indicative of the harm or potential harm caused by its breach in this case. The period of YBS's breach was from 1 November 2009 to 17 June 2012. The total revenue derived by YBS from the sale of the Cliquet Product during this period was £18,559,696.

6.8 In deciding on the percentage of the relevant revenue that forms the basis of the Step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 20%. The range is divided into five fixed levels which represent, on a sliding scale, the seriousness of the breach; the more serious the breach, the higher the level. For penalties imposed on firms, there are the following five levels:

Level 1 – 0%

Level 2 – 5%

Level 3 – 10%

Level 4 – 15%

Level 5 – 20%

6.9 In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, which include:

1) whether the breach had an effect on particularly vulnerable people, whether intentionally or otherwise (DEPP 6.5A.2G(6)(d));

2) the frequency of the breach (DEPP 6.5A2G(7)(b)); and

3) whether the firm, in committing the breach, took any steps to comply with FSA rules, and the adequacy of those steps (DEPP 6.5A.2G(7)(h)). The Authority has taken into account that, by 24 September 2010, the prominence of the maximum return in the YBS Financial Promotions had been reduced, which resulted in a marked improvement in their overall presentational balance.

6.10 DEPP 6.5A.2G(9) lists the factors that tend to show that the breach was reckless including whether the firm's senior management, or a responsible individual, appreciated that there was a risk that their actions or inaction could result in a breach and failed adequately to mitigate that risk.

6.11 DEPP 6.5A.2G(11) lists factors likely to be considered 'level 4 or 5 factors'. In assessing the seriousness of the misconduct, the Authority considers the relevant factor to be whether YBS was aware there was a risk that the content of its financial promotions failed to meet the requirement to be clear, fair and not misleading, but took inadequate steps to mitigate the risk.

6.12 DEPP 6.5A.2G(12) lists factors likely to be considered 'level 1, 2 or 3 factors'. Of these, the Authority considers the following factors to be relevant:

1) there is no evidence that the breach indicates a widespread problem or weaknesses at the firm; and

2) there was no, or limited, actual or potential effect on the orderliness or confidence in markets, as a result of the breach.

6.13 Taking all of these factors into account, the Authority considers the seriousness of the breach to be level 3 and so the Step 2 figure is 10% of £18,559,696.

6.14 The figure at Step 2 is therefore £1,855,970.

Step 3: mitigating and aggravating factors

6.15 Pursuant to DEPP 6.5A.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including any amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breach.

6.16 The Authority considers that the following factors aggravate the breach:

1) that previous guidance from the Authority stressed the importance of clarity and balance in financial promotions. Those guidance documents included:

   a. Financial Promotions: taking stock and moving forward (February 2005);

   b. Capital secured structured products (2005 review, updated April 2010);

   c. Responsibilities of Providers and Distributors for the Fair Treatment of Customers" ("RPPD") (July 2007);

   d. Financial Promotions Industry Update No.3 – Stand-alone compliance (September 2009);

   e. Thematic Review: Structured Products (October 2009);

   f. Financial Promotions – guidance Prominence (September 2011); and

   g. Retail Product Development and Governance – Structured Products Review (Guidance Consultation) (November 2011).

2) the changes made by YBS in September 2010 to reduce the prominence of the maximum return in its financial promotions were made at the instigation of third parties, including the Authority and Which?, rather than on YBS's own initiative.

6.17 The Authority considers that the following factors mitigate the breach:

1) the level of co-operation shown by YBS both when the issue was raised by the Authority during the issue of one of the tranches (PCA 40) and subsequently;

2) the agreement by YBS to extend the customer contact exercise; and

3) the changes made to the Product Brochures after June 2012.

6.18 The Authority has considered the various aggravating and mitigating factors, and having done so considers that the Step 2 figure should be subject to a 10% uplift at Step 3.

6.19 Therefore, the Step 3 figure is £2,041,567.

Step 4: adjustment for deterrence

6.20 Pursuant to DEPP 6.5A.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.

6.21 The Authority considers that the Step 3 figure represents a sufficient deterrent to YBS and others, and so has not increased the penalty at Step 4.

6.22 The figure at Step 4 therefore remains £2,041,567.

Step 5: settlement discount

6.23 Pursuant to DEPP 6.5A.5G, if the Authority and the firm on whom a penalty is to be imposed agree the amount of the financial penalty and other terms, DEPP 6.7 provides that the amount of the financial penalty which might otherwise have been payable will be reduced to reflect the stage at which the Authority and the firm reached agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.

6.24 The Authority and YBS reached agreement at Stage 1 and so a 30% discount applies to the Step 4 figure.

6.25 The figure at Step 5 is therefore £1,429,097 which has been rounded down to £1,429,000.

Penalty

6.26 The Authority therefore imposes a total financial penalty of £1,429,000 on YBS for breaching Principle 7 and BCOBS Rules 2.3.1R and 4.1.1R.

7. PROCEDURAL MATTERS

Decision maker

7.1 The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.

7.2 This Final Notice is given under, and in accordance with, section 390 of the Act.

Manner of and time for payment

7.3 The financial penalty must be paid in full by YBS to the Authority by no later than 30 June 2014, 14 days from the date of the Final Notice.

If the financial penalty is not paid

7.4 If all or any of the financial penalty is outstanding on 1 July 2014, the Authority may recover the outstanding amount as a debt owed by YBS and due to the Authority.

Publicity

7.5 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 Authority must publish such information about the matter to which this notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to you or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

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

Authority contacts

7.7 For more information concerning this matter generally, contact Pritheeva Rasaratnam (direct line: 020 7066 9806) of the Enforcement and Financial Crime Division of the Authority.

Signed:

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Jamie Symington

Financial Conduct Authority, Enforcement and Financial Crime Division

ANNEX A

RELEVANT STATUTORY AND REGULATORY PROVISIONS

1. STATUTORY PROVISIONS

1.1 The Authority’s operational objectives, set out in sections 1B to 1E of the Act, are to secure an appropriate degree of consumer protection, to protect and enhance the integrity of the UK financial system and to promote effective competition in the interests of consumers.

1.2 Section 206(1) of the Act provides:

“If the appropriate regulator considers that an authorised person has contravened a relevant requirement imposed on the person, it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate."

2. REGULATORY PROVISIONS

Principles for Business (PRIN)

2.1 The Principles are a general statement of the fundamental obligations of firms under the regulatory system and are set out in the Authority’s Handbook. They derive their authority from the Authority’s rule-making powers as set out in the Act and reflect the Authority’s regulatory objectives. The Principles relevant to this case are as follows:

2.2 Principle 7 states:

“A firm must 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.”

Handbook Rules

2.3 The Authority’s Banking Conduct of Business Sourcebook (BCOBS) has applied to authorised firms since 1 November 2009. It sets out the Authority’s rules governing the activity of accepting deposits from banking customers carried on from an establishment maintained by it in the United Kingdom and activities connected with accepting deposits. It includes sections on communicating with banking customers, including those relating to financial promotions.

2.4 BCOBS 2.3.1R provides:

"A firm must ensure that each communication made to a banking customer and each financial promotion communicated or approved by the firm:…

(2) is accurate and, in particular, does not emphasise any potential benefits of a retail banking service without also giving a fair and prominent indication of any relevant risks;

(3) is sufficient for, and presented in a way that is likely to be understood by, the average member of the group to whom it is directed, or by whom it is likely to be received; and

(4) does not disguise, diminish or obscure important information, statements and warnings."

2.5 BCOBS 4.1.1R provides:

"A firm *must provide or make available to a banking customer appropriate information about a retail banking service and any deposit made in relation to that retail banking service:*

(1) in good time;

(2) in an appropriate medium; and

(3) in easily understandable language and in a clear and comprehensible form;

so that the banking customer can make decisions on an informed basis."

The Decision Procedure and Penalties Manual ("DEPP")

2.6 Chapter 6 of DEPP, which forms part of the Authority's Handbook, sets out the Authority's statement of policy with respect to the imposition and amount of financial penalties under the Act.

The Enforcement Guide

2.7 The Enforcement Guide sets out the Authority's approach to exercising its main enforcement powers under the Act.

2.8 Chapter 7 of the Enforcement Guide sets out the Authority's approach to exercising its power to impose a financial penalty.