Financial Conduct Authority

FINAL NOTICE

To: **Chase de Vere Independent Financial Advisers Limited (formerly AWD Chase de Vere Limited) ("CdV")**

Firm Reference Number: **137914**

Address: **60 New Broad Street**
London
EC2M 1JJ

Date: **5 November 2014**

1. ACTION

1.1. For the reasons given in this notice, the Authority hereby imposes on CdV a financial penalty of £560,000. This action is in respect of breaches of Principles 3 and 7, SYSC 3.2.6R and certain applicable rules set out in COB and COBS.

1.2. This notice relates solely to CdV's conduct and does not make any criticism of Keydata or any person other than CdV.

1.3. CdV agreed to settle at an early stage of the Authority's investigation. CdV 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 £800,000 on CdV.

2. SUMMARY OF REASONS

2.1. CdV sold a total of 3,846 Keydata Products to 2,806 customers between August 2005 and June 2009 ("the relevant period"). The total amount invested by CdV's customers was £49.3 million. The Keydata Products were based on investments in corporate bonds which were issued by SPVs incorporated in Luxembourg. The funds raised through the issue of the bonds (i.e. the amount invested by retail customers in the products through Keydata) were then invested in a portfolio of US life insurance policies and cash.

2.2. Throughout the relevant period, in breach of Principle 3 and SYSC 3.2.6R, CdV failed to put in place adequate systems and controls to ensure that the distinctive features of the Keydata Products were researched to an adequate standard, to understand the risks they posed to investors and to ensure that these risks were properly understood by the firm's advisers. CdV also failed to put in place adequate risk management systems to mitigate the risk that its advisers would fail to describe the Keydata Products in a way that was clear, fair and not misleading.

2.3. In addition, throughout the relevant period, CdV failed to disclose to its customers certain distinctive features and risks of the Keydata Products in a way which was clear, fair and not misleading, in breach of Principle 7 and certain applicable Rules set out in COB and COBS.

2.4. As a result of these breaches, the Authority considers there is a risk that investors' decisions to invest in the Keydata Products were based on information regarding the distinctive features and risks of the Keydata Products which was not clear, fair and not misleading.

2.5. The Authority regards these failings as being serious for the following reasons:

a. The misconduct occurred in respect of a series of Keydata Product tranches which CdV recommended to 2,806 customers over a period of almost four years;

b. 139 customers invested a total of £4.4 million in Keydata Products in excess of the FSCS compensation limit applicable at the time;

c. The breaches revealed systemic weaknesses in CdV's internal controls, so that inadequate research led to a failure to impose restrictions on sales of Keydata Products and a failure to disclose appropriately the distinctive features and risks of the Keydata Products to investors; and

d. Despite being made aware of the risks of ceasing to provide linkage for structured products in June 2006, CdV failed to take adequate and timely steps to assess and mitigate those risks. Linkage was ultimately reintroduced in October 2008.

2.6. The Authority has taken into account the fact that CdV has taken action to improve certain aspects of its business including its business quality monitoring, sales practices, systems and controls, product research, management information, compliance monitoring and complaints handling during and after the relevant period. This factor mitigates the seriousness of CdV's failings.

2.7. CdV has agreed to undertake a review process in respect of those customers who have not made a claim against FSCS or CdV concerning their investment in the Keydata Products and will provide redress where appropriate.

2.8. This action supports the Authority's consumer protection objective.

3. DEFINITIONS

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

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

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

"ATR" means attitude to risk, or the degree of risk that a customer is willing to accept in connection with the purchase of an investment product

"CdV" means Chase de Vere Independent Financial Advisers Limited, which was previously known as AWD Chase de Vere Limited

"COB" means the Conduct of Business Sourcebook, which formed part of the Authority's Handbook and which was in force until 31 October 2007

"COBS" means the Conduct of Business Sourcebook, which forms part of the Authority's Handbook and was in force from 1 November 2007

"DEPP" means the Authority's Decision Procedure and Penalties Manual

"DIP" means the Defined Income Plan 1, 2, 3, 4, 5, 6, 7, 8 and 9

"EG" means the Authority's Enforcement Guide

"ENF" means the Authority's Enforcement Sourcebook, which formed part of the Authority's Handbook and which was in force until 27 August 2007

"FOS" means the Financial Ombudsman Service

"FSCS" means the Financial Services Compensation Scheme

"IFA" means Independent Financial Adviser

"Keydata" means Keydata Investment Services Limited (now dissolved)

"Keydata Products" means products offered by Keydata that were based on investments in corporate bonds which were issued by special purpose vehicles incorporated in Luxembourg. The funds raised through the issue of the bonds (i.e. the amount invested by retail customers in the products through Keydata) were then invested in a portfolio of predominantly US life insurance policies and cash

"Lifemark" means Lifemark SA, the SPV incorporated in Luxembourg which issued bonds backing the Secure Income Bond 4, the Secure Income Plan and the Defined Income Plan

"Principles" means the Authority's Principles for Businesses set out in PRIN 2.1.1 R (Principles for Businesses) of the Authority's Handbook

"relevant period" means August 2005 to June 2009

"SCARP" means Structured Capital at Risk Product

"SIB" means the Secure Income Bond 1, 2, 3 and 4 (the first Keydata Products offered by CdV)

"SIP" means the Secure Income Plan 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12 and 14

"SLS" means SLS Capital SA, the SPV incorporated in Luxembourg which issued bonds backing the Secure Income Bond 1, 2 and 3

"SPV" means a special purpose vehicle

"SYSC" means the Systems and Controls Sourcebook, which forms part of the Authority's Handbook

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

"Traded Life Policy Investments" or "TLPI" means pooled investments in life assurance policies sold either directly or indirectly through other investments such as funds of funds

4. FACTS AND MATTERS

4.1. CdV is a large IFA firm with 182 advisers and branches in a number of UK locations. During the relevant period it offered financial advice to retail customers through advisers based in its branches and through a client services team, which offered financial advice over the telephone.

4.2. In April 2005, CdV was an amalgam of businesses which had recently been brought together by merger and takeover. The two main constituent parts of the entity were:

a. Thomson's – a national financial adviser business which was re-branded to the AWD Group in October 2004; and

b. Chase de Vere – a UK-wide financial adviser business acquired by the AWD Group in March 2005.

CdV's Keydata sales

4.3. During the relevant period, CdV sold a total of 3,846 Keydata Products to 2,806 customers. The total amount invested by CdV's customers was £49.3 million.

4.4. CdV generated a total of £1,633,053.85 in commission (£1,317,581.22 in gross initial commission and £315,472.63 in trail commission) from the sale of Keydata Products during the relevant period. As a result of the sums CdV has paid to customers and to the FSCS, CdV has not benefited financially from its sales of the Keydata Products.

The Keydata Products

4.5. Keydata was an authorised product provider that designed and distributed structured investment products both directly and via an extensive network of IFAs. The Keydata Products offered investors an income or growth investment, by way of Individual Savings Account, Personal Equity Plan or direct investment. The income option paid a specified percentage income (payable monthly, quarterly or annually) and aimed to ensure the full return of capital to the investor at the end of a five, seven or ten year term. The growth option rolled up and reinvested the income payments to provide compound growth over the life of the product and similarly aimed to provide full return of capital at the end of the term.

4.6. The Keydata Products were Traded Life Policy Investments ("TLPI") based on investments in corporate bonds. On behalf of investors, Keydata purchased bonds which were issued by SPVs incorporated in Luxembourg. The funds raised through the issue of the bonds (i.e. the amount invested by retail customers in the products through Keydata) were then invested by the SPV in a portfolio of US life insurance policies and cash. The Keydata Product marketing materials stated that the investment mix was intended to be 60% policies/ 40% cash for the bonds issued by SLS, and 70% policies/ 30% cash for the bonds issued by Lifemark. SLS and Lifemark each purchased life insurance policies taken out predominantly by US citizens, paid the premiums due on those policies, and collected the maturity payment due under the policy when the individual died.

Distinctive features of the Keydata Products

4.7. Product material provided to CdV by Keydata revealed that there were a number of significant distinctive features, including the following:

a. Although the Keydata Products were intended to return capital in full at the end of the investment period, they offered no capital guarantee, and put all capital invested at potential risk;

b. Successful performance of the Keydata Products depended on the accuracy of an actuarial model used by Keydata. Significant technological or pharmaceutical development could affect the accuracy of the model and when insurance policies were likely to mature;

c. The bonds had a fixed term of five, seven or ten years. This meant that Keydata undertook to return funds to investors on the date when the bond matured, even if, at that point in time, it had insufficient funds because the insured individuals were living longer than anticipated;

d. The underlying life insurance policy assets were not traded on an exchange in the way that stocks and shares are. The risk existed that, if it became necessary to sell an insurance policy to make funds available, this might take longer than anticipated, and might only be possible at a reduced value, reducing the value of the portfolio;

e. The Keydata Products involved investment in a single specialist asset class (predominantly US senior life insurance policies) through a single issuer (at first SLS, then Lifemark). Although a percentage of the investment was to be held in cash, this was not held as a separate investment, but was intended to be used to pay the insurance premiums, income payments and operational costs associated with the investment; and

f. The Keydata Products had a significant international dimension: the underlying assets were predominantly US life insurance policies, and the issuers of the bonds were based in Luxembourg. As the bond issuer was offshore, customers would not have recourse to the FSCS statutory compensation scheme in the event of default of the bond issuer.

CdV's assessment of the distinctive features of Keydata Products

Research process for structured products

4.8. During the relevant period, CdV had a centralised Research team. The Research team was responsible for maintaining selections of products approved for sale, known as "product panels", including a panel for structured products. Advisers had either to recommend products from a product panel, or, if they wanted to recommend a product which was not on panel, to follow an off-panel request process.

4.9. For part of the relevant period the Research team was also responsible for drafting standard descriptions of products on CdV's product panel for use by advisers in written communications to customers including descriptions of the features and risks of the products.

4.10. In the case of structured products, the Research team considered new products following guidance set out in a Research Procedures manual before deciding whether or not to approve them on to the structured products panel.

4.11. The March 2005 Research Procedures manual (which was in force at the start of the relevant period) described structured products as follows:

> "*Structured Products involve the underlying use of derivatives to create the structure of the investment. Products are usually available on a tranche basis and the risk/return payoff depends on the current level of interest rates and stockmarket [sic] volatility.*"

4.12. The Keydata Products did not fit CdV's description of typical structured products set out above because their structure did not involve a derivative, and the returns they sought to achieve were not linked to an index but to the proceeds of a portfolio of life policies.

4.13. Where the Research team encountered a product which it considered did not fit with CdV's standard approach, it could escalate the decision whether or not to approve the product to a committee whose membership comprised individuals from the Research, Compliance and Wealth Management areas of the business, including members of the firm's senior management. At the start of the relevant period, the relevant committee was the Advice Suitability Group ("ASG"); from January 2008, the ASG was replaced by the Investment Steering Group ("ISG").

Approval of SIB 1 onto structured products panel

4.14. The Research team recognised that the first of the Keydata Products, SIB 1, was novel in that it combined life settlement funds with the form of a structured product. A member of the Research team therefore referred the product by email to the ASG for their consideration on 22 July 2005. Members of ASG discussed the product by exchange of emails between 22 July 2005 and 26 July 2005. The product was added to CdV's structured products panel on 8 August 2005 with the approval of the ASG. While CdV's expectation is that the ASG would have met to approve the product, the firm has been unable to produce the minutes of any meeting of the ASG at which SIB 1 was approved. The reasons for approving SIB 1 appear from the email correspondence and from interviews the investigation team conducted with members of CdV's Research team to have been:

a. CdV had an older, income-seeking client base. SIB 1 offered diversification from equities and fixed interest products;

b. SIB 1's rate of income was attractive in the context of falling interest rates;

c. The product was tax-efficient; and

d. While the product involved risks, they were "not huge".

4.15. On 25 July 2005, during the approval process, one member of the ASG informed the Research team that he was concerned that the client-facing literature did not explain how the product's returns were achieved. He noted that AWD was not convinced that life settlement funds were sufficiently well understood to be sold compliantly and that, following the same approach as it did with viatical funds and hedge funds, AWD had made a conscious decision not to support such recommendations. CdV has been unable to produce any evidence recording whether this concern was addressed by the Research team prior to the product's addition to panel on 8 August 2005, nor whether it was shared with the ASG's wider membership.

4.16. CdV could not provide details of what research was undertaken, although it expected that it would have involved a review of the product literature and speaking to Keydata in order to determine the key risks involved and complete a standard product checklist. The only relevant risk listed on the checklist was that capital was not guaranteed. CdV has been unable to produce any records of any other research or due diligence carried out into SIB 1 by the Research team prior to the ASG's decision to approve it.

Research and approval of subsequent Keydata Products

4.17. The approach taken by CdV when considering subsequent tranches of the Keydata Products was to check whether the latest tranche had any differences from the previous tranche and, if there were any, to query these with Keydata. The original decision to approve the Keydata Products in principle was never revisited. The Research team approved subsequent tranches of Keydata Products without further reference to the ASG or the ISG. Over the course of the relevant period, CdV approved 26 Keydata Products on to its structured products panel.

4.18. The evidence does not show that either the Research team or the ASG analysed the risks of the Keydata Products or investigated the mitigating factors sufficiently to carry out an adequate risk assessment on them. The Authority considers that the process underlying the research, assessment and approval of the Keydata Products was insufficiently rigorous.

Limits on sale of Keydata Products

4.19. CdV did not generally risk rate individual products or set limits on sales of individual products, either by reference to a minimum ATR for a customer to be recommended the product or a maximum percentage of a customer's portfolio that could be invested in it. As a rule, once a product had been accepted onto its panel it was left to individual advisers' judgement to decide to whom to sell the product and in what amounts based on each customer's individual circumstances, needs and objectives.

4.20. CdV employed an asset allocation model, which guided advisers on how to distribute a customer's funds between four asset classes (cash, fixed interest, commercial property, equities). The limits set by this model on different asset classes may have served indirectly to limit the concentration of investment in particular products because a customer's maximum investment in a particular product might be limited to the maximum concentration in the category to which the product belonged under the model. CdV recognised that the Keydata Products did not fit within the firm's asset allocation model or its definition of typical structured products (as noted above).

4.21. CdV did apply direct restrictions on sales of certain categories of products. For products it categorised as "alternative and uncorrelated assets", CdV set a minimum customer ATR of 6 out of 10 and a maximum concentration of 15% for recommendations. CdV did not consider the Keydata Products to fall within the alternative and uncorrelated assets category so they were not subject to these restrictions.

4.22. From 1 October 2008, CdV introduced a rule that structured products could not be recommended to customers with an ATR below 5 out of 10. The Keydata Products were an exception to this rule and could be recommended to customers with an ATR of 4 out of 10.

4.23. On 28 April 2009, in response to changes to the underlying actuarial assumptions, CdV introduced further restrictions on sales of TLPI:

a. TLPI could not be recommended to customers with a lower ATR than the product risk rating (this was 4 out of 10 in the case of DIP 9, the Keydata Product on sale at the time);

b. A maximum of 5% of a customer's portfolio could be invested in any single product provider; and

c. All recommendations of the products required approval from a sales manager prior to use.

These restrictions were put in place shortly before Keydata was placed into administration and the Keydata Products were withdrawn from sale. As a result, they were too late to have any meaningful effect.

4.24. The Authority considers that had CdV researched the Keydata Products to an adequate standard, it would have recognised from the outset (as it ultimately did recognise) that their distinctive features presented different risks to any other structured products CdV offered, and for that reason they should have been subject to controls on their sale to lower risk customers, over and above the limits on asset concentration indirectly provided by the asset allocation model. These controls could have included all or any of the following measures:

a. Broadening the classification of alternative and uncorrelated assets to include the Keydata Products;

b. Setting a minimum customer ATR for investment in the Keydata Products;

c. Setting a maximum percentage of a customer's portfolio that could be invested in the Keydata Products; and/or

d. Requiring that recommendations of Keydata Products should involve an additional level of approval, e.g. by a sales manager, prior to use.

4.25. The Authority notes that although in most of the customer files it reviewed CdV recommended that customers invest a relatively low proportion of their portfolio in Keydata Products, in a small number of cases CdV's advisers exposed customers to excessive concentration risk.

CdV’s risk disclosures to customers

Information provided to advisers

4.26. CdV’s advisers were provided with the following information to assist them in understanding the risks associated with the Keydata Products:

a. Technical training at branch sales meetings including training given by representatives of Keydata;

b. Product literature produced by Keydata;

c. Structured product checklists produced by the Research team, which presented a summary of key facts for each product; and

d. Suggested wording (known as “linkage”) to be used when describing the Keydata Products and their associated risks in suitability reports provided to customers. Advisers could access linkage through a tool used to draft suitability reports, called “Report Writer”. Linkage was provided during some parts of the relevant period but not others, as detailed further below.

Production of linkage

4.27. Until about June 2006, the Research team was responsible for drafting linkage and obtaining approval for it from CdV’s Compliance department before it was issued to advisers. The Research team produced linkage for SIB 1, 2 and 3 (but not SIB 4), and SIP 1 and 2. CdV has not been able to identify whether or not the linkage for SIB 3 received approval from Compliance; the linkage for SIB 1 and 2 and SIP 1 and 2 did. During this period, advisers were not obliged to use the linkage, and were able to add or remove information or write their own product descriptions and risk disclosures if they wished.

Decision to cease providing linkage

4.28. By March 2006, CdV’s Compliance function lacked sufficient resources to review the Research team’s structured product linkage within the agreed timescales. CdV’s Research team had also identified that advisers were composing their own wording independently when describing structured products.

4.29. In approximately June 2006, CdV decided to cease providing linkage and so from then the Research team did not provide advisers with any linkage for the Keydata Products. CdV staff realised the risks of ceasing to provide linkage and escalated them to senior management but linkage was not reinstated until October 2008.

4.30. Despite being aware of the risks, there is no evidence that CdV took adequate and timely steps to assess and mitigate the risks of ceasing to provide linkage. After the issue was escalated to him, a member of CdV’s Compliance department said that it had not been possible for the senior management team to reconsider it in the time available as other issues had arisen. He observed that linkage had not been provided for several months without there being any “serious business impediment”.

4.31. The Authority’s investigation team reviewed 33 suitability letters in which CdV’s advisers recommended Keydata Products, 32 of which were written prior to 1 October 2008 (when linkage was re-instated).

a. In six suitability letters, advisers made significant changes to the linkage and added statements to their suitability letters that were factually inaccurate, as detailed further in paragraphs 4.43 to 4.44 below.

b. In 22 suitability letters, advisers used out of date versions of the linkage.

c. In six suitability letters, advisers omitted one of the main features of the Keydata Products, that it was susceptible to actuarial risk, by omitting the following statement in the linkage: "*Your capital may be at risk if factors change which affect the rate at which insurance contracts mature*".

Reinstatement of linkage

4.32. From around October 2008, CdV decided to reintroduce linkage for structured products including the Keydata Products, and to make it compulsory for advisers to use it.

Capital protection

4.33. The linkage for SIB 1 included the following statement which suggested that the Keydata Products offered capital protection:

> "*You should be aware that with this investment, although your capital is protected, it is <u>not</u> guaranteed.*"

4.34. The Authority notes that Keydata's product literature for SIB 1 did not say that investors' capital was "protected". The Keydata Products did not offer any capital protection and investors were at risk of losing all their money if the products did not perform as intended.

4.35. The above statement appeared in CdV's linkage for SIB 1-3 and SIP 1 and 2, although it was removed from the linkage for DIP 6-9. For the period from June 2006 to October 2008 when no linkage was provided, most advisers continued to include a statement that capital was protected in suitability letters until linkage was provided for DIP 6 in October 2008.

4.36. This statement appeared in 23 of the 33 suitability letters reviewed by the Authority.

Actuarial risk

4.37. The successful performance of the Keydata Products depended on the accuracy of an actuarial model used by Keydata. There was a risk that significant technological or pharmaceutical developments could impact on the accuracy of the model and when insurance policies were likely to mature.

4.38. The following statements in the linkage for SIB 1 and 2 related to the actuarial risk:

> "*A financial model, developed in conjunction with KPMG, determines the blend of cash and insurance contracts at any one time. The model will be reviewed regularly and rebalanced where appropriate*"

> "*The value of your investment will be at risk should the KPMG financial model be inaccurate.*"

4.39. The following statement in the linkage for SIB 3 and SIP 1 and 2 related to the actuarial risk:

> "*Your capital may be at risk if factors change which affect the rate at which insurance contracts mature.*"

4.40. CdV's linkage for DIP 6-9 stated the following in respect of the actuarial risk:

> "*Your capital may be at risk if factors change which affect the rate at which insurance contracts mature. The actuarial modelling used to provide the financial model is based on recognised industry standards. There is a risk that a significant technological or pharmaceutical development could impact on the accuracy of the model and when the contracts are likely to mature. This could result in reductions in the value of contracts or delayed cash flow which could mean that capital might not be returned in full at the end of the term.*"

4.41. The Authority considers that CdV's linkage for SIB 1-3 and SIP 1 and 2 failed to describe the nature of the actuarial risk sufficiently clearly for investors to be able to give it appropriate consideration prior to investing in the Keydata Products. While the linkage for DIP 6-9 described the nature of the actuarial risk more clearly than previous iterations, it failed to explain that the return of not only an investor's capital, but also any growth or income generated by the investment was uncertain and depended on accurate life expectancy estimates.

4.42. CdV failed to describe the actuarial risk sufficiently clearly in all 33 of the 33 suitability letters reviewed by the Authority.

Other risk disclosures

4.43. In the period prior to October 2008 when CdV made the use of linkage mandatory, CdV had no controls in place which would prevent the use of misleading risk disclosures in suitability letters prior to their being issued. The Authority identified six letters within the sample of 33 suitability letters it reviewed that contained misleading statements which were not included in the linkage for the corresponding issue of the product:

a. In four of the 33 suitability letters the adviser described the Keydata Product as a "*cash based product…that will provide you with a higher level of income than your standard savings accounts without taking a high level of risk.*" While the Keydata Products were intended to keep a proportion of an investor's money in cash, neither the Keydata Product brochure nor CdV's linkage described them as "cash based". While each of these suitability letters later stated that the Keydata Product was linked to a portfolio of cash and traded life insurance policies, the above was not an accurate description of the product. Three of these four letters also gave the FSCS cover limits applicable to deposit accounts, which were not the limits which applied to the Keydata Products.

b. In another letter, an adviser stated that: "*The Keydata Secure Income Plan offers the trust a very high level of capital security and a guaranteed income of 7.5% for five years…There is no investment risk attached to this product…*" In fact, none of the Keydata Products offered investors a guaranteed income and there were numerous risks associated with the products that could affect the security of investors' capital.

c. In a further letter, an adviser stated that: "*…On death there could be a loss of capital. As these are tangible and highly sought after assets one would expect that they are traded at around par and hence little, if any, capital loss would be expected…*" As noted above, the insurance policies underlying the Keydata Products were not traded on an exchange and were potentially illiquid. It was misleading to suggest that they would be expected to trade "at around par".

4.44. In nine of the 33 suitability letters reviewed, the adviser omitted the section of the linkage containing risk disclosures relevant to the recommended Keydata Product altogether.

5. FAILINGS

5.1. The regulatory provisions relevant to this Final Notice are referred to in the Annex.

5.2. As a result of the facts and matters stated at paragraphs 4.8 to 4.42 above, the Authority considers that CdV breached Principle 3:

a. Throughout the relevant period, CdV failed to put in place adequate systems and controls to ensure that the distinctive features of the Keydata Products were researched to an adequate standard to understand the risks they posed to investors and to ensure they were understood by the firm's advisers;

b. CdV also failed to put in place adequate risk management systems to ensure that its advisers would describe the Keydata Products in a way that was clear, fair and not misleading:

i. Between the start of the relevant period and 1 June 2006 and again between 1 October 2008 and the end of the relevant period, the linkage CdV provided to advisers failed to describe the Keydata Products in a way that was clear, fair and not misleading. As a result, even when advisers followed the firm's processes and used approved linkage, their suitability letters breached the Authority's rules.

ii. Between 1 June 2006 and 1 October 2008, the decision to cease providing linkage was taken without sufficient regard to the risks involved, despite the firm's awareness of the potential risks of leaving advisers to write their own product descriptions without specific guidance.

5.3. For the same reasons, CdV also breached SYSC 3.2.6R throughout the relevant period.

5.4. As a result of the facts and matters stated at paragraphs 4.33 to 4.44 above, the Authority considers that CdV breached Principle 7 throughout the relevant period. CdV failed to disclose to its customers the distinctive features and the consequent risks of the Keydata Products in a way which was clear, fair and not misleading. For the same reasons, CdV also breached COB 2.1.3R and COBS 2.2.1R, 4.5.2R and 14.3.2R during the periods referred to in the Annex.

6. SANCTION

6.1. The Authority's policy on whether to issue a financial penalty is set out in Chapter 6 of DEPP.

6.2. Changes to DEPP were introduced on 6 March 2010. As CdV's misconduct occurred prior to that date, the Authority has had regard to the provisions of DEPP in force prior to 6 March 2010.

6.3. In determining the appropriate level of financial penalty the Authority has also had regard to Chapter 13 of ENF for the part of the Relevant Period up until 27 August 2007 (the last date ENF was in force) and Chapter 7 of EG thereafter. The Authority's approach to taking disciplinary action is set out in Chapter 2 of EG.

6.4. In determining whether a financial penalty is appropriate, the Authority is required to consider all the relevant circumstances of the case. DEPP 6.5.2G sets out a non-exhaustive list of factors which may be relevant in this respect. The Authority considers the following DEPP factors to be particularly important in assessing the sanction for CdV's breach of Principle 3, Principle 7 and the applicable SYSC, COB and COBS rules.

Deterrence: DEPP 6.5.2G (1)

6.5. The principal purpose of a financial penalty is to promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter others from committing similar breaches and demonstrating generally the benefits of compliant business.

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

6.6. In determining the appropriate sanction, the Authority has had regard to the seriousness of the breaches by CdV, including the duration and frequency of the breaches and whether the breaches revealed serious failings in CdV's systems and controls, as well as the loss or risk of loss caused to customers.

6.7. CdV's breaches were serious. 139 customers invested a total of £4.4 million in Keydata Products in excess of the FSCS compensation limit applicable at the time.

6.8. CdV's breaches also revealed systemic weaknesses in the firm's internal controls, with advisers systematically failing to use the firm's most up to date risk disclosures for Keydata Products and, where they did use them, frequently omitting to disclose one of the key risks associated with the products, actuarial risk.

The extent to which the breach was deliberate or reckless: DEPP 6.5.2G (3)

6.9. The Authority has not determined that CdV deliberately or recklessly contravened regulatory requirements.

The size, financial resources and other circumstances of the person on whom the penalty is to be imposed: DEPP 6.5.2G (5)

6.10. The Authority has taken into account the size and financial resources of CdV. There is no evidence to suggest that CdV is unable to pay the penalty.

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

6.11. As a result of the sums CdV has paid to customers and to the FSCS, CdV has not benefited financially from its sales of the Keydata Products.

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

6.12. The Authority imposed a financial penalty of £1.12 million on CdV in November 2008 (the "2008 Notice") for breaches of Principle 9 and Principle 3 arising from systemic weaknesses in the firm's compliance systems and controls in relation to its pension transfer, pension annuity and income withdrawal business in the period between 28 February 2006 and 31 October 2007. The consequence of the breaches was that CdV failed to treat certain of its customers fairly.

Other action taken by the Authority: DEPP 6.5.2G (10)

6.13. In determining the level of financial penalty, the Authority has taken into account penalties imposed on other authorised firms for comparable behaviour.

6.14. CdV has agreed to settle at an early stage of the Authority's investigation, and therefore qualifies for a 30% (Stage 1) discount under the Authority's executive settlement procedures.

6.15. The Authority therefore hereby imposes a financial penalty of £560,000 on CdV for breaching Principle 3 and Principle 7. Were it not for the Stage 1 settlement discount, the Authority would have imposed a financial penalty of £800,000 on CdV.

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 CdV to the Authority by no later than 19 November 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 20 November 2014, the Authority may recover the outstanding amount as a debt owed by CdV 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 Matthew Hendin (direct line: 020 7066 0236 /fax: 020 7066 0237) of the Enforcement and Financial Crime Division of the Authority.

Bill Sillett

Project Sponsor
Financial Conduct Authority, Enforcement and Financial Crime Division

ANNEX

RELEVANT STATUTORY PROVISIONS, REGULATORY REQUIREMENTS AND AUTHORITY GUIDANCE

1. Relevant statutory provisions

1.1. The Authority's statutory objectives are set out in section 2(2) of the Act. In relation to this case, the most relevant statutory objective is the protection of consumers.

1.2. Section 206(1) of the Act provides:

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

CdV is an authorised person for the purposes of section 206(1) of the Act. The requirements imposed on authorised persons include those set out in the Authority's Principles and Rules made under section 138 of the Act.

2. Relevant Handbook provisions

2.1. In exercising its power to issue a financial penalty, the Authority must have regard to the relevant provisions in the Authority's Handbook.

2.2. In deciding on the above action, the Authority has also regard to guidance published in the Authority's Handbook and set out in the Regulatory Guides, in particular DEPP.

Principles for Businesses

2.3. Principle 3 provides:

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

2.4. Principle 7 provides:

"*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.*"

Conduct of Business Rules

2.5. The Authority has issued Rules under section 138 of the Act relating to the conduct of investment business, including relating to advising customers to purchase investment products. These are set out in COB for products sold before 1 November 2007 and COBS for products sold from 1 November 2007.

<u>For sales prior to 1 November 2007</u>

2.6. COB 2.1.3R provides:

"*When a firm communicates information to a customer, the firm must take reasonable steps to communicate in a way which is clear, fair and not misleading.*"

<u>For sales on or after 1 November 2007.</u>

2.7. COBS 2.2.1R provides:

(1) A firm must provide appropriate information in a comprehensible form to a client about:

(a) the firm and its services;

(b) designated investments and proposed investment strategies; including appropriate guidance on and warnings of the risks associated with investments in those designated investments or in respect of particular investment strategies;

(c) execution venues; and

(d) costs and associated charges;

so that the client is reasonably able to understand the nature and risks of the service and of the specific type of designated investment that is being offered and, consequently, to take investment decisions on an informed basis.

(2) That information may be provided in a standardised format.

2.8. COBS 4.5.2R provides:

A firm must ensure that information:…

(2) is accurate and in particular does not emphasise any potential benefits of relevant business or a relevant investment 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 items, statements or warnings.

2.9. COBS 4.5.4G provides:

In deciding whether, and how, to communicate information to a particular target audience, a firm should take into account the nature of the product or business, the risks involved, the client's commitment, the likely information needs of the average recipient, and the role of the information in the sales process.

2.10. COBS 4.5.5G provides:

When communicating information, a firm should consider whether omission of any relevant fact will result in information being insufficient, unclear, unfair or misleading.

2.11. COBS 14.3.2R provides:

A firm must provide a client with a general description of the nature and risks of designated investments, taking into account, in particular, the client's categorisation as a retail client or a professional client. That description must:

(1) explain the nature of the specific type of designated investment concerned, as well as the risks particular to that specific type of designated investment, in sufficient detail to enable the client to take investment decisions on an informed basis; and

(2) include, where relevant to the specific type of designated investment concerned and the status and level of knowledge of the client, the following elements:

(a) the risks associated with that type of designated investment including an explanation of leverage and its effects and the risk of losing the entire investment;

(b) the volatility of the price of designated investments and any limitations on the available market for such investments;

(c) the fact that an investor might assume, as a result of transactions in such designated investments, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the designated investments; and

(d) any margin requirements or similar obligations, applicable to designated investments of that type.

Systems and Controls Rules

2.12. SYSC 3.2.6R provides:

A firm must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system and for countering the risk that the firm might be used to further financial crime.