Demetrios Hadjigeorgiou and David Stephen have referred their Decision Notices to the Upper Tribunal where they will each present their respective cases. Any findings in these individuals' Decision Notices are therefore provisional and reflect the FCA's belief as to what occurred and how it considers their behaviour is to be characterised.

Kulvir Virk has not referred the FCA's decision to the Upper Tribunal and his Final Notice has not been the subject of any judicial finding. To the extent that Kulvir Virk's Final Notice contains criticisms of Demetrios Hadjigeorgiou and David Stephen, they have received Decision Notices which set these out. They dispute many of the facts and any characterisation of their actions in Kulvir Virk's Final Notice and have referred their Decision Notices to the Upper Tribunal for determination. The Tribunal's decision in respect of the individuals' references will be made public on its website.

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DECISION NOTICE

To: David John Alexander Stephen

Reference Number: DJS01438

Date: 25 April 2024

1. ACTION

1.1. For the reasons given in this Decision Notice, the Authority has decided to:

(1) impose on David John Alexander Stephen a financial penalty of £52,100 pursuant to section 66 of the Act; and

(2) make an order prohibiting Mr Stephen from performing any senior management function and significant influence function in relation to any regulated activities carried on by any authorised or exempt person, or exempt professional firm pursuant to section 56 of the Act.

2. SUMMARY OF REASONS

2.1. On the basis of the facts and matters described below, the Authority considers that between 3 January 2018 and 2 August 2019 (the "Relevant Period"), Mr Stephen breached Statement of Principle 1 (Integrity) and Statement of Principle 6 (Due skill, care and diligence) of the Authority's Statements of Principle and Code of Practice for Approved Persons Chapters of the Authority's Handbook ("APER") by failing to act with integrity and by failing to exercise due skill, care and diligence in managing the business of SVS Securities Plc ("SVS").

2.2. During the Relevant Period, Mr Stephen was the Head of Risk and Compliance at SVS and held the controlled functions of CF10 (Compliance Oversight) and CF11 (Money Laundering Reporting). SVS operated a discretionary fund management business that managed investments held on behalf of retail pension customers within a self-invested personal pension ("SIPP"). The pension funds within the SIPPs were then invested into one of four portfolios of assets created and managed by SVS (the "Model Portfolios"). The Model Portfolios were called Income / Mixed / Growth / Aggressive Growth and SVS's marketing material described them as being *'high risk portfolios designed to give you maximum growth opportunities'.*

2.3. Discretionary fund managers act as agents for their customers, making investment decisions in financial markets on their behalf. Confidence that discretionary fund managers will conduct themselves properly when acting on behalf of customers is central to the relationship of trust between the industry and its customers. When making investment decisions for customers, discretionary fund managers should act in the best interests of their customers and should not let conflicts of interest interfere with their obligations to customers. The Authority has stressed the importance of discretionary fund managers managing conflicts of interest effectively.

2.4. A business model was operated at SVS that maximised the flow of retail customer funds into the Model Portfolios for onward investment into high-risk illiquid bonds operated by connected persons and business associates of SVS. This model, which inappropriately prioritised income to SVS at the expense of the firm's customers, operated throughout the Relevant Period and was driven by the financial benefit

that SVS derived from commissions of up to 12% of the customer's investment, paid to SVS out of the principal which SVS customers invested in the bonds.

2.5. SVS entered into a series of commission-driven commercial arrangements with these bond operators that committed SVS to channel customer funds into the high-risk fixed income bonds. The model relied upon incentivising unauthorised introducers through marketing agreements by which SVS paid these introducers commission of 7-9% of the introduced customer's funds that were invested into SVS's Model Portfolios. A total of 879 customers invested £69.1 million into the Model Portfolios. Over half of these customers were advised to invest in SVS by a financial adviser firm that was wholly or partly controlled by the owners of one of the introducers to whom SVS was secretly paying incentive commission.

2.6. At a time when SVS had financial concerns, and in order to generate more income, SVS decided to apply a 10% mark-down on the valuation that customers would receive when they disinvested from the fixed income assets in the Model Portfolios. This mark-down was not notified to existing or prospective investors. Mr Stephen actively supported the implementation of the decision yet chose to dismiss multiple concerns raised with him that the mark-down was not fair to customers. As a consequence, he was reckless regarding these concerns and the known risk that customers would be treated unfairly.

2.7. Mr Stephen was aware that the purpose of the mark-down was to generate revenue for SVS. Indeed, SVS earned £359,800 in income at the expense of its customers. Despite knowing of the concerns over the risks to customers, Mr Stephen nonetheless chose to support the arrangement.

2.8. Furthermore, he recklessly failed to take steps to ensure that SVS complied with regulatory standards both in terms of the change and its communications to customers or their financial advisers. This meant that customers were detrimentally affected, as they did not have the opportunity to consider the potential impact of the mark-down when deciding to disinvest. Even when a disclosure was eventually made to customers by SVS, some six months later, as Mr Stephen well knew, it did not specify the 10% mark-down.

2.9. SVS considered the Model Portfolios to be high risk products. However, Mr Stephen failed to take reasonable steps to ensure that only customers with a high attitude to risk were accepted by SVS. He was aware that financial advisers advised lowest medium and high medium risk customers to invest in the Model Portfolios yet took no action to address the risk this created for those customers: instead of taking reasonable steps to ensure that SVS properly assessed for

appropriateness by determining the needs, characteristics and objectives of the Model Portfolio customers, Mr Stephen as CF10 unreasonably relied on financial advisers to do this. As a result of this failure, SVS continued to accept customers from financial advisers even though the Model Portfolios had a higher level of risk than these customers were willing or able to bear.

2.10. Mr Stephen failed to take reasonable steps to ensure that SVS complied with the Authority's rules in relation to inducements. SVS received large commission payments from fixed income product providers in return for including their investments in the Model Portfolios. This represented a level of inducement which put at risk SVS's independence and compromised its ability to act in the best interests of its customers. COBS 2.3A.15R, which came into force on 3 January 2018, states that a firm must not accept any commission from any third party in provision of a relevant service to retail clients. As the Head of Risk and Compliance Mr Stephen should have ensured that SVS did not accept such payments after 3 January 2018.

2.11. The Authority has concluded that in respect of the matters in paragraphs 2.6 to 2.8, Mr Stephen failed to act with integrity, in breach of Statement of Principle 1, and that in respect of the matters in paragraphs 2.9 to 2.10, he failed to exercise due skill, care and diligence in managing the business of SVS, in breach of Statement of Principle 6.

2.12. In addition, as a result of his conduct, the Authority considers that Mr Stephen is not a fit and proper person, and he poses a risk to consumers and to the integrity of the financial system. The nature and seriousness of the breaches outlined above warrant the imposition of an order prohibiting him from performing any senior management function or significant influence function in relation to any regulated activities carried on by an authorised or exempt person or exempt professional firm.

2.13. Further, the Authority considers it appropriate to impose a financial penalty on Mr Stephen of £52,100 for his breaches of Statement of Principle 1 and Statement of Principle 6 during the Relevant Period.

3. DEFINITIONS

3.1. The definitions below are used in this Notice:

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

"Mr Anderson" means Stuart James Anderson.

"Angelfish" means Angelfish Investments Plc.

"APER" means the Statements of Principle and Code of Practice for Approved Persons.

"the Authority" means the Financial Conduct Authority.

"CFBL" means Corporate Finance Bonds Limited.

"CFBL Bonds" means various series of bonds issued by CFBL under its £500m secured note programme, launched on 21 June 2016.

"COBS" means the part of the Authority's Handbook entitled "Conduct of Business Sourcebook".

"DEPP" means the Decision Procedure and Penalties Manual part of the Authority's Handbook.

"EG" means the Authority's Enforcement Guide set out in the Authority's Handbook.

"FIT" means the Fit and Proper Test for Approved Persons and specified significant-harm functions section of the Authority's Handbook.

"the FSCS" means the Financial Services Compensation Scheme.

"the Handbook" means the Authority's Handbook of rules and guidance.

"ICFL" means Innovation Capital Finance Limited.

"ICFL Bond" means the bond issued by ICFL under its £100m secured note programme, launched on 17 January 2019, in respect of which SVS made an investment of £10m.

"IFA" means Independent Financial Adviser.

"Ingard" means Ingard Limited.

"Ingard Alternative Funding" means Ingard Alternative Funding Limited.

"Ingard Financial" means Ingard Financial Limited.

"Ingard Property Bond 1" means the bond issued by Ingard Property Bond Designated Activity Company.

"Ingard Property Bond 2" means the bond issued by Ingard Property Bond 2 Designated Activity Company.

"Ingard Property Bonds" means Ingard Property Bond 1 and Ingard Property Bond 2.

"Investment Committee" means the committee providing oversight on discretionary and advisory services offered, it handles the products in the model portfolio and monitors the investment performance.

"Mark-down" means the difference, if any, between:

(i) the price at which the firm takes a principal position in the relevant investment in order to fulfil a customer order; and

(ii) the price at which the firm executes the transaction with its customer.

"MiFID II" means the Markets in Financial Instruments Directive (2014/65/EU).

"Model Portfolios" means the discretionary fund managed model portfolios managed by SVS.

"Model Portfolio Team" means the SVS staff responsible for the Model Portfolios.

"OC Finance" means OC Finance S.A.

"OC Finance Bonds" means bonds issued by OC Finance.

"PROD" means the part of the Authority's Handbook entitled "Product Intervention and Product Governance Sourcebook".

"Prohibition Order" means the order to be made pursuant to section 56 of the Act prohibiting Mr Stephen from performing any senior management function and any significant influence function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm.

"Queros" means Queros Capital Partners PLC.

"RDC" means the Regulatory Decisions Committee of the Authority (see further under Procedural Matters below).

"the Relevant Period" means the period between 3 January 2018 and 2 August 2019.

"SIPP" means a self-invested personal pension. A SIPP is the name given to the type of UK government-approved personal pension scheme, which allows individuals to make their own investment decisions from the full range of investments approved by Her Majesty's Revenue and Customs.

"SIPP Trustee" means the trustee and administrator of the SIPPs used to invest in the Model Portfolios.

"Specialist Advisors" means Specialist Advisors Limited.

"the Statements of Principle" means the Statements of Principle as set out in APER.

"Mr Stephen" means David John Alexander Stephen.

"SVS" or "the firm" means SVS Securities Plc.

"SYSC" means the part of the Authority's Handbook entitled "Senior Management Arrangements, Systems and Controls".

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

"Mr Virk" means Kulvir Virk.

"the Warning Notice" means the Warning Notice dated 17 February 2023 given to Mr Stephen.

4. FACTS AND MATTERS

Background

4.1. SVS was regulated by the Authority from 9 April 2003 to 31 August 2023. It had permission under Part 4A of the Act to carry out a range of regulated advisory and transactional activities. Its principal business activities included: advising on investments, dealing in investments as agent, dealing in investments as principal, managing investments, arranging safeguarding and administration of assets, and safeguarding and administration of assets.

4.2. SVS's four main services, or business areas, were:

1) Advisory - traditional stockbroking services (private client broking) on an advisory basis to both retail and Institutional clients. This also included taking part in AIM listings and secondary placings on a principal basis;

2) Discretionary - investments into the Model Portfolios by one of the SVS discretionary team;

3) Execution only - online equity, ISA, SIPP trading on an execution only basis; and

4) Foreign exchange trading - Retail online execution only foreign exchange business that operated under the trading name of SVSFX.

4.3. Mr Stephen was first approved by the Authority to perform the CF10 (Compliance Oversight) and CF11 (Money Laundering Reporting) functions at SVS on 6 August 2014. He held these roles during the Relevant Period. His responsibilities included providing the decision-making framework for responding to, and adjudicating, third party queries and complaints. Mr Stephen was also responsible for responding to all information requests from the Authority, including in relation to the Model Portfolio.

4.4. The Authority received a number of complaints from customers about the Model Portfolios in early 2019. On 13 May 2019, the Authority requested that SVS provide information about the due diligence that it had conducted on investments within its Model Portfolios. On 2 July 2019, the Authority conducted a site-visit at SVS's offices.

4.5. The information gathered by the Authority from SVS raised serious concerns and on 26 July 2019, at the request of the Authority, SVS applied for requirements to be imposed on it. Requirements were imposed on the firm on the same date. Under the voluntary requirements SVS agreed to cease all regulated activities in relation to its discretionary fund management business and not to accept any new customers into, or invest any fixed income provides in, any of its other business areas.

4.6. On 2 August 2019, the Authority imposed further requirements on SVS requiring it to cease all regulated activities, safeguard assets and notify affected third parties.

4.7. On 5 August 2019, SVS was placed into Special Administration. The Special Administration ended on 30 March 2023 and SVS was dissolved on 10 August 2023.

4.8. The FSCS started considering claims from Model Portfolio customers on 10 August 2020.

The Model Portfolios and Underlying Investments

Creation and Structure of the Model Portfolios

4.9. During the Relevant Period, 879 retail customers invested £69.6 million in the Model Portfolios. The vast majority of the customers who invested in the Model Portfolios were retail customers transferring their pensions from existing pension plans, including customers who had transferred from defined benefit pension schemes.

4.10. The Model Portfolios were created by SVS as part of its discretionary fund management business. The Model Portfolios were broken down into four separate portfolios: Income, Mixed, Growth and Aggressive Growth. They purported to invest in a mixture of equities, fixed income and collective funds which could be tailored to meet different customer objectives. Of the total £69.6 million invested in the Model Portfolios, around 73% of the invested monies were allocated to the fixed income products.

Governance of the Model Portfolios

4.11. The SVS Board of Directors was responsible for *'oversight and overview'* of the Model Portfolios.

4.12. Separate from the Board of Directors, there were a number of committees with formal governance responsibilities for the Model Portfolios. These included a Model Portfolio Strategic Investment Committee (the "Investment Committee"), a Fixed Income Investment Committee, a FTSE Investment Committee, a Small Cap Investment Committee and a Funds / Yield Investment Committee. Mr Stephen was not a member of any of these committees. As Head of Compliance and Risk, he was responsible for approving all marketing materials, and for providing advice on the form and content of customer statements and the future strategy of the Model Portfolios.

4.13. The Model Portfolio Team had overall responsibility for the Model Portfolios, convening Investment Committee meetings, producing management information, devising and implementing operational strategy, ensuring that introducer and financial advisers were *'properly serviced',* dealing with disinvestments, and onboarding new clients.

Features of the Model Portfolios

4.14. The Model Portfolios were discretionary managed portfolios which aimed to deliver a strategy of capital growth and income through asset allocation.

4.15. By July 2019, the fixed income asset class comprised the following high risk, corporate bonds and preference shares:

1) CFBL Bonds;
2) Ingard Property Bonds;
3) ICFL Bond;
4) Angelfish preference shares; and
5) Queros.

CFBL Bonds

4.16. At the start of the Relevant Period, SVS had already invested Model Portfolio funds into the OC Finance Bonds, which were fixed income products. In 2016, Mr Anderson established CFBL as a new vehicle to attract fixed income investment. CFBL issued a £500 million secured note programme which launched on 21 June 2016. The stated aim of the programme was to provide UK companies with development capital to grow their business - through accelerated growth plans, acquisitions or realisation of new opportunities. It purported to achieve this by issuing bonds and then using the capital to lend to such businesses on a secured basis.

4.17. The CFBL £500 million secured note programme was approved by the Irish Stock Exchange on 21 June 2016. Each series of the CFBL Bonds was listed on the Global Exchange Market of Euronext Dublin. The OC Finance Bonds, into which SVS had already invested Model Portfolio funds, were rolled into the CFBL Bond programme as Series 1 and Series 2. There were eight different series of the CFBL Bonds. The bonds were issued with a fixed rate of interest (either 5.95% or 6.25%) for a fixed term of 4.5 or 5 years. The CFBL Bonds had maturity dates between 7 July 2021 and 24 April 2022.

4.18. Between 16 February 2016 and 1 July 2019, SVS invested into six series of the CFBL Bonds. As at 1 July 2019, a total of £23,912,255 of SVS customer funds was invested in the CFBL Bonds via the Model Portfolios. This represented 29% of all funds in the Model Portfolios. Over half of the fixed income investments in the Model Portfolios were invested in CFBL Bonds.

4.19. In return for investing SVS customer funds into the CFBL Bonds, CFBL paid SVS commission of 10-12% of the funds invested. The CFBL Bonds were delisted on 6 November 2019 due to the economic environment and to save costs.

4.20. By 29 April 2020, the CFBL Bonds had defaulted on coupon payments. With effect from 18 May 2020, Heritage Corporate Finance Ltd replaced CFBL as the issuer of the bonds. Customers are only expected to recover between 20-35% of the value of their investments in the CFBL Bonds.

Ingard Property Bonds

4.21. SVS included Ingard Property Bond 1 and Ingard Property Bond 2 in the Model Portfolios. The stated purpose of both bonds was to provide bridging loans to the UK property market. Both bonds were listed on the Cyprus Stock Exchange.

4.22. Both bonds were issued with a fixed rate of interest (either 5.75% or 7%) for a fixed term of 7 years. Ingard Property Bond 1 matured on 31 December 2023 and Ingard Property Bond 2 is due to mature on 31 December 2025. In January 2017 SVS invested Model Portfolio customer funds into Ingard Property Bond 1 and in December 2017, SVS invested Model Portfolio customer funds into Ingard Property Bond 2, in each case in return for commission of 12% of the customer funds invested. As at 1 July 2019, SVS had invested £5.7 million into the Ingard Property Bonds. This represented 7% of the total funds in the Model Portfolios.

ICFL Bond

4.23. ICFL issued a £100 million secured note programme which launched on 17 January 2019. The stated aim of the programme was to facilitate secured lending, primarily in the innovation and technology sector. The purpose of the ICFL Bond was to connect investors seeking high, fixed income yields with capital security, and borrowers seeking capital injections at competitive rates to grow their business.

4.24. As at 1 July 2019, SVS had invested £10 million in the ICFL Bond in the Model Portfolios, in return for commission of 10% of customer funds invested. The bond was issued for a fixed term until 30 January 2024 with a fixed 6.25% coupon. As at 1 July 2019, there were £9,802,834 of Model Portfolio customer funds invested in the ICFL Bond, which represented 12.3% of the total funds in the Model Portfolios. ICFL Bonds comprised 23.09% of all the fixed income investments in the Model Portfolios.

Angelfish Preference Shares

4.25. SVS invested just over £3 million in Angelfish preference shares within the Model Portfolios. Angelfish's investment strategy was focused on businesses and companies in the technology sectors, and the stated purpose of the preference share issue was to progress development activities and provide capital for further investment opportunities as they arose. The preference shares were listed on the NEX Exchange Growth Market in the UK. As at 11 May 2016, SVS invested into the Angelfish preference shares. Subsequently SVS purchased a further tranche of preference shares in October 2018. A commission was paid to SVS of 9-10% on the October 2018 Model Portfolios' take up of preference shares issued by Angelfish. There was no historic trading activity in the Angelfish preference shares before SVS invested. As at 1 July 2019, SVS had £3,065,447 of Model Portfolio customer funds invested into the Angelfish Preference Shares, which represented 3.65% of the total funds in the Model Portfolios.

4.26. The Angelfish preference shares offered dividends at 7.1% per annum. Angelfish has defaulted on dividend payments and no payment has been received by customers since 30 June 2019. The Angelfish preference shares were converted to ordinary shares in September 2020.

The Customer Journey

4.27. SVS operated a business model that relied upon financial incentives to market its discretionary managed Model Portfolios to retail customers. SVS then used those customer funds for its own benefit by exercising its discretion to prefer fixed income investments which paid SVS itself substantial commission, calculated as a percentage of the customer funds that SVS steered into those investments.

Unauthorised Introducers

4.28. SVS entered into marketing agreements with unauthorised introducer firms and individuals. The role of the introducer was to "generate certain customer lead types … with a view to generating income" for SVS. SVS incentivised its introducers to attract customers funds into the Model Portfolios by paying them commission calculated as a percentage of the net sum invested with SVS. This incentive commission varied between 7% and 9% of customer funds invested, depending on the introducer.

4.29. Mr Stephen was aware of the potential risks of this business model as, on 4 August 2016, he emailed an Authority alert to the directors of SVS which highlighted the responsibilities of authorised firms when accepting business from unauthorised

introducers, particularly where the introducer influences the final investment choice.

Financial Advisers

4.30. The introducer firms did not introduce customers directly to SVS; they introduced prospective customers to financial advisers on the premise that they would recommend the Model Portfolios to customers where it was suitable to do so.

4.31. The unauthorised introducers introduced customers to financial advisers employed by various regulated financial advice firms; prospective customers were introduced for a pension review.

4.32. SVS had written Introducing Broker Partnership Agreements with the financial advice firms. The terms of the Introducing Broker Partnership Agreements included that the financial advisers would only introduce customers to SVS for whom the services could reasonably be expected to be suitable.

SIPP Trustees

4.33. For those customers that were advised to invest in the Model Portfolios, SIPP Trustees would enter into an arrangement with the customer to maintain a SIPP and to hold its assets. The SIPP Trustees were clients of SVS and established, operated and administered the SIPPs.

4.34. The financial advisers were responsible for contacting the SIPP Trustees on behalf of the customer.

SVS (Discretionary Fund Manager)

4.35. SVS categorised the Model Portfolio customers as retail customers. SVS made discretionary decisions on which assets to include in the Model Portfolios. Each of the Model Portfolios held the same assets but in different proportions. Customers were not asked for permission before investing, but they and their financial advisers would receive statements on a periodic basis detailing the investments.

Decision to introduce a mark-down on fixed income disinvestments

4.36. The Authority requires firms to pay due regard to the interests of their customers and treat them fairly. This obligation was acknowledged in SVS's Order Execution Policy.

Decision to introduce a 10% mark-down

4.37. In November 2018, the Board of Directors decided to introduce a 10% mark-down on the valuation of the fixed income assets when a customer disinvested from the Model Portfolios. The rationale provided in contemporaneous internal documentation for taking a 10% mark-down was to earn additional income for SVS.

4.38. This decision was made by the SVS Board of Directors supported by Mr Stephen. In actively supporting the decision and implementing it whilst dismissing the internal concerns about its fairness which were raised by SVS staff, Mr Stephen failed to prevent SVS from treating customers unfairly. Moreover, the application of a 10% mark-down was not notified to customers. This meant that customers did not have the opportunity to consider the potential impact of the mark-down when deciding whether to disinvest. If customers knew about this charge, they may have decided to disinvest before it came into effect or not to disinvest after it had, both of which would have led to less income for SVS. As such, Mr Stephen played an important role in an arrangement that he knew was designed to generate revenue for SVS to the detriment of its customers.

Failure to communicate the 10% mark-down to customers

4.39. Prior to November 2018, SVS did not charge customers when they disinvested from the Model Portfolios.

4.40. From November 2018, SVS applied a 10% mark-down on all fixed income disinvestments. This mark-down was applied to all customers who disinvested regardless of the length of time they had held their investment. This was contrary to the statement in the Model Portfolio brochure provided to customers (which Mr Stephen, as Head of Compliance, was responsible for), that exit charges to customers who disinvested would differ based on the length of time a customer had been invested.

4.41. In breach of COBS 11.2A.31R, SVS did not communicate the 10% mark-down to customers in a clear manner and did not disclose anything in writing to customers, their SIPP Trustees or financial advisers for a further six months, namely on 30 May 2019. The written disclosure that was eventually made only referred to "the wider spread"; it did not include any reference to the fixed 10% mark-down, but referred instead to a "spread", at Mr Stephen's suggestion. The Authority considers the reference to the mark-down as a spread by Mr Stephen to be misleading as the reference to the fixed 10% mark-down was not referable to specific bid/offer prices in the market but was instead applied as 10% to all disinvestments that took place from November 2018. In addition to this,

contemporaneous correspondence (copied to Mr Stephen) demonstrates that the Model Portfolio Team understood the mark-down to operate as a fixed charge.

Internal concerns regarding the introduction of the 10% mark-down

4.42. Staff within SVS raised concerns that, amongst other things, the decision to introduce a 10% mark-down was not fair to customers and would lead to complaints. Despite these concerns being raised with Mr Stephen and the SVS Board of Directors a number of times, they were unreasonably disregarded by Mr Stephen and he continued to support the 10% mark-down and as a result failed to prevent SVS from treating customers unfairly.

4.43. Concerns were raised to Mr Stephen and directors in relation to the introduction of the 10% mark-down, and/or the operation of the process behind the 10% mark-down, on the following occasions:

1) 2 November 2018 – concerns were raised about SVS profiting unduly from a disinvestment mark-down which was higher than the proposed exit charge;

2) 19 November 2018 - concerns were raised about not having a *"fully formed procedure"*;

3) 22 November 2018 - concerns were raised that the introduction of the 10% mark-down was not *"a workable solution"*;

4) 26 November 2018 – staff within SVS questioned the justification for applying a 10% mark-down;

5) 11 December 2018 - concerns were raised that SVS was double counting costs charged to customers;

6) 14 December 2018 – concerns were raised that the 10% mark-down "*looks like a fee coming straight out of the models*";

7) 17 December 2018 – concerns were raised that the situation was unworkable and SVS was unable to provide an explanation to customers that could be defended;

8) 4 February 2019 – concerns were raised that the disinvestment process was not fair on customers; and

9) 13 February 2019 – concerns were raised that the new disinvestment policy was *"not an efficient way to carry out the disinvestments when compared to*

the application of exit charges as a percentage that reduces with each year of participation."

4.44. Mr Stephen did not consider the concerns raised to be valid. Mr Stephen suggested that the mark-down could be explained as falling within the best execution rules, although concerns had been raised to him about that. In supporting the 10% mark-down and dismissing the concerns raised about it, Mr Stephen failed to prevent SVS from treating customers unfairly by applying a fixed charge to all disinvestments which was not notified to customers. This meant that customers did not have the opportunity to consider the potential impact of the mark-down when deciding whether and when to disinvest.

4.45. Mr Stephen sent internal SVS emails in November and December 2018 referring to the concerns raised as *"ridiculous"* and reiterated that the decision to implement the 10% mark-down had been made and he had approved it. For example, Mr Stephen stated in an email in November 2018 *"As far as I'm concerned the main reason for the delays have been the* [Model Portfolio Team's] *continual procrastination over the disinvest process despite this being agreed both by email and at meetings on a number of occasions. As you can see below* [Model Portfolio Team member] *is again questioning what the process is ... it's ridiculous!!".* Mr Stephen dismissed the concerns raised within SVS about the 10% mark-down without giving appropriate consideration to the issues raised.

Financial consequences for customers due to the introduction of the 10% mark-down

4.46. SVS prioritised its profits at the expense of customers by introducing a 10% mark-down on the value of fixed income disinvestments. After the decision was made to introduce the 10% mark-down, customers disinvested £5,784,000 between October 2018 and August 2019. From these disinvestments, SVS earned £359,800 in income as customers were charged a higher amount than the cost to SVS. This income would have increased had SVS not entered administration on 5 August 2019.

4.47. The table below sets out the consequences of the introduction of the 10% mark-down for three customers:

	Customer 94008	**Customer 84848**	**Customer 124128**
Amount invested	£92,890.92	£266,204.76	£20,296.10
Date of investment	16 June 2017	1 November 2016	20 February 2019
Date disinvestment actioned	4 February 2019	4 February 2019	13 March 2019
Value of investments at date of disinvestment **(A)**	£75,575.54	£223,575.15	£19,880.64
Amount returned to customer **(B)**	£71,132.62	£210,431.09	£18,645.93
Amount returned to customer (%) **(B / A)**	94%	94%	94%
Value of fixed income assets disinvested **(C)**	£35,904.41	£106,214.79	£7,029.93
Amount of fixed income assets returned to customer **(D)**	£32,314.01	£95,593.33	£6,326.97
Fixed income disinvestment mark-down **(C – D)**	£3,590.40	£10,621.46	£702.96
Fixed income disinvestment mark-down (%) **(D / C)**	10%	10%	10%
Fixed income disinvestment as % of total investment **(C-D / A)**	5%	5%	4%

4.48. Customer 94008 was 60 years old when they invested, was a carer to their elderly parent, owned a property worth £70,000, had an annual income of £4,700, and had other investments of £7,000. The Authority considers that the fixed income disinvestment mark-down of £3,590.40 taken by SVS was a significant amount to the customer.

4.49. Customer 84848 planned to retire in 10 years, was a personal assistant earning around £31,000 a year, owned a property worth £185,000, and had other savings

and investments of £2,100. The Authority considers that the fixed income disinvestment mark-down of £10,621.46 taken by SVS was a significant amount to the customer. Customer 84848 submitted a complaint to SVS due to the performance of the Model Portfolios, the customer statements being unclear, and unsatisfactory service received from SVS. In the complaint, Customer 84848 explicitly asked whether exit charges were applied, to understand why the value of the customer's investment had decreased. The response to the complaint, signed by or on behalf of Mr Stephen, claimed that the Firm did not apply exit charges and instead the reduction in value was due to the "*wider spread*" on fixed income products when sold "*into the market*". This misrepresented the situation to the customer as a flat 10% had been applied to the disinvestment, which operated as charge. In reviewing the complaint, SVS considered that compensation may be appropriate for the unsatisfactory service provided but it does not appear that the firm considered the amount that the customer lost due to the disinvestment mark-down applied.

4.50. Customer 124128, and their partner, invested all of their pension funds of £20,296 into the Model Portfolio and had no other savings or investments. The customer planned to retire within 10 years, was a road maintenance worker earning £30,000 a year, and jointly owned a property worth £500,000. The customer was only invested in the Model Portfolios for 3 weeks and lost £702.96 due to the disinvestment mark-down, which the Authority considers to be a significant amount to the customer.

Summary

4.51. The decision to introduce a 10% mark-down on all fixed income disinvestments was strongly supported by Mr Stephen and was not made with the best interests of customers in mind. In particular, the decision was made to generate revenue for SVS at a time when the firm had financial concerns, and it unduly prioritised the interests of the firm over the interests of customers.

4.52. Furthermore, SVS did not inform customers in writing of the change until six months after the change had been made, and the disclosure did not specify that SVS was taking a 10% mark-down. Concerns about the process were raised by the Model Portfolio Team but were not handled appropriately by Mr Stephen who unreasonably dismissed the concerns rather than addressing the fairness issues which had been raised.

4.53. The Authority considers that Mr Stephen actively supported the decision to apply a 10% mark-down at the expense of retail pension customers; he did not deal

with the concerns raised in an appropriate manner; and he did not take reasonable steps to ensure that the decision was communicated to customers or their financial advisers in a durable format.

High level of fees and commission received by SVS

4.54. SVS received high levels of commission from the Model Portfolio fixed income product providers. COBS 2.3A.15R came into force on 3 January 2018, in line with MiFID II, relates to the payment of inducements including commission. It states that a firm must not accept any commission from any third party in provision of a relevant service to retail clients. However, throughout the Relevant Period, SVS was paid commission from product providers calculated as a percentage of the customer funds SVS directed to that product. This incentivised SVS to maximise the investment of customer funds into these products. Mr Stephen should have ensured that SVS did not accept such payments. These inducements put at risk SVS's independence and compromised its ability to act in the best interests of its customers.

4.55. When SVS placed customer funds into the Fixed Income investments, it received the following commission:

1) in relation to investments in CFBL, SVS received 10% commission from CFBL and 2% from Specialist Advisors. This investment totalled £23,436,165, or 54.41% of the Fixed Income investments;

2) in relation to investments in the Ingard Property Bonds, SVS received 10% commission from Ingard Alternative Funding and 2% from Ingard Financial. This investment totalled £5,700,000, or 13.23% of the Fixed Income investments;

3) in relation to investments in ICFL, SVS received 10% commission. SVS drew down £750,000 of the £1 million commission upfront due to liquidity and cashflow issues. This investment totalled £9,802,834, or 22.76% of the Fixed Income investments;

4) in relation to an investment in Angelfish preference shares in October 2018, SVS received 9%-10% commission. This investment totalled £3,065,447, or 7.12% of the Fixed Income investments; and

5) in relation to investments in Queros, SVS did not receive any commission. This investment totalled £1,067,093 or 2.48% of the Fixed Income Investments.

4.56. The amounts invested by SVS in the fixed income investments corresponded with the amount of commission generated. The largest fixed income investments in the Model Portfolios were the CFBL Bonds, for which SVS received the greatest amount of commission. The smallest fixed income investment in the Model Portfolios was Queros, for which SVS received no commission.

4.57. The additional 2% paid to SVS on investments in CFBL and the Ingard Property Bonds was also determined by reference to the amount of customer funds invested by SVS in the relevant product.

4.58. The commission paid to SVS by the fixed income product providers was used to pay the marketing fees to the introducer firms to incentivise them to steer new customers into the Model Portfolios.

4.59. The commission payments expressed as a percentage of the customer funds invested into the product, together with the trigger for payment (channelling investor funds into bond products) that arose after 3 January 2018 were accordingly in breach of COBS 2.3A.15R. The Authority has found no evidence to indicate that the commission payments SVS received were necessary for the services it provided.

4.60. Mr Stephen was aware of the commission paid by the fixed income product providers to SVS and provided this information to the Authority in response to an information requirement dated 11 May 2017. As the holder of the firm's CF10 (Compliance Oversight) function, the Authority considers that Mr Stephen should have ensured that the firm fully considered the implications of COBS 2.3A.15R following its introduction so as to remain compliant after 3 January 2018 with the Authority's rules in relation to inducements.

4.61. SVS charged commission of 1.5% on all transactions, which was reduced to 0.75% in April 2019. Taking into account the IFA advice fee of up to 4% of the customer's investment, this meant that Model Portfolio customers lost up to 5.5% of their investment at the outset. As SVS also took up to 10% of its customer's funds for commission in respect of fixed income products, this increased the risk of product default, so the likelihood that Model Portfolio customers would get back what they paid in was reduced further.

Notifying customers about the risk of the Model Portfolios

Risk of the Model Portfolios

4.62. Section 3.3.1R of PROD which came into force on 3 January 2018, states that a distributor must: understand the financial instruments it distributes to clients; assess the compatibility of the financial instruments with the needs of the clients to whom it distributes investment services, taking into account the manufacturer's identified target market of end clients; and ensure that financial instruments are distributed only when this is in the best interests of the client. SVS was a distributor for purposes of the PROD rules.

4.63. SVS considered the Model Portfolios to be high risk products. It was SVS's responsibility to ensure that the customer understood the risk of the investment. Approximately 90% of SVS's Model Portfolio customers received pension switching or pension transfer advice. Despite this, SVS did not take sufficient steps to identify groups of end customers for whose needs, characteristics and objectives the Model Portfolio was not compatible. This is despite the provisions of PROD 3.3.15R(3) which require such steps to be taken. SVS instead relied on the assessments carried out by each end customer's financial adviser.

4.64. SVS was provided with the financial advisers' suitability letters for customers. These letters disclosed customers' attitudes to risk and included customers whose attitudes to risk were not classed as high (such as lowest medium risk or high medium risk). As the Model Portfolios were considered to be high risk, these customers had invested in products with a higher level of risk than they may have been willing or able to bear. Mr Stephen was aware of this. While SVS carried out appropriateness checks on new customers, these were limited and lacked adequate independent assessment, relying instead on the suitability advice that was given to customers by financial advisers. As a result, SVS Compliance, led by Mr Stephen, allowed large numbers of retail pension customers to invest their savings into the high-risk Model Portfolios.

4.65. Mr Stephen did not address the risk to customers from SVS failing in its obligation to act in its customers' best interests and to carry out adequate assessment that would identify and exclude customers for whose needs the Model Portfolios were not suitable; Mr Stephen knew that SVS continued to accept customers even though the Model Portfolios had a higher level of risk than these customers were willing or able to bear.

5. FAILINGS

5.1. The statutory and regulatory provisions relevant to this Notice are referred to in Annex A.

5.2. Based on the facts and matters described above, and for the reasons set out below, the Authority considers that during the Relevant Period Mr Stephen breached Statement of Principle 1 and Statement of Principle 6.

Breach of Statement of Principle 1

5.3. Mr Stephen breached Statement of Principle 1 during the Relevant Period because he failed to act with integrity in carrying out his accountable functions.

5.4. Mr Stephen's actions, in actively supporting the decision to introduce a 10% mark-down to the valuation of fixed income disinvestments, led to SVS's customers not being treated fairly and suffering detriment:

1) Multiple concerns were raised to Mr Stephen by the Model Portfolio Team over the course of action relating to the mark-down as not being fair to customers, yet he chose to dismiss these, rather than addressing the fairness issues which had been raised;

2) Mr Stephen was aware that the purpose of the mark-down was to generate more income for SVS, at a time when it had financial concerns, at the expense of retail pension customers. SVS earned £359,800 in income at the expense of its customers. He supported the arrangement despite the concerns raised by the Model Portfolio Team; and

3) Mr Stephen failed to take steps to ensure that the change was adequately communicated to customers or their financial advisers. As a consequence, from the time their disinvestment decision was taken, customers were detrimentally affected as they did not have the opportunity to consider the potential impact of the mark-down when deciding to disinvest. In particular, when a disclosure was eventually made to customers, some six months later, as Mr Stephen well knew, it did not specify the 10% mark-down.

5.5. As a result of the above failings, during the Relevant Period, Mr Stephen failed to act with integrity in carrying out his accountable functions. He was reckless as to the risk to customers from the 10% mark-down, with the result that his actions directly led to SVS customers being adversely impacted whilst SVS benefitted financially.

Breach of Statement of Principle 6

5.6. Mr Stephen breached Statement of Principle 6 during the Relevant Period because he failed to exercise due skill, care and diligence in managing the business of SVS. Mr Stephen:

1) was aware that financial advisers advised lowest medium and high medium risk customers to invest in the Model Portfolios which were high risk products. However, contrary to the Authority's rules after 3 January 2018, he failed to take reasonable steps to address the risk this created for customers: instead of ensuring that SVS properly assessed for appropriateness by determining the needs, characteristics and objectives of the Model Portfolio customers, Mr Stephen relied on financial advisers to do this. As a result of this failure, SVS continued to accept customers from financial advisers even though the Model Portfolios had a higher level of risk than these customers were willing or able to bear; and

2) was aware of the amount of commission received by SVS from the fixed income product providers, an inducement which was contrary to the Authority's rules after 3 January 2018, put at risk SVS's independence and compromised its ability to act in the best interests of its customers. Mr Stephen therefore failed to take reasonable steps to ensure that the firm complied with the Authority's rules in relation to inducements.

5.7. As a result of the above failings, during the Relevant Period, Mr Stephen failed to exercise due skill, care and diligence in managing the business of SVS, with the result that SVS's customers were adversely impacted whilst SVS benefitted financially.

Fit and Proper test for Approved Persons

5.8. The Authority and consumers rely on senior management function holders to ensure that authorised firms are properly managed and comply with the requirements of the regulatory regime. Mr Stephen's failings were not confined to just one part of SVS's business but occurred in a range of areas for which, as CF10, he held specific responsibilities: Mr Stephen failed to prevent SVS treating customers unfairly with the introduction of the disinvestment mark-down—with the result that customers disinvesting from the Model Portfolio suffered financial detriment; and failed to ensure that SVS complied with rules governing the payment of inducements.

5.9. By reason of the facts and matters described above, the Authority considers that Mr Stephen's conduct demonstrates a serious lack of integrity, and competence and capability, such that he is not a fit and proper person to perform any senior management function or significant influence function in relation to regulated activities carried on at any authorised person, exempt person or exempt professional firm.

6. SANCTION

Financial penalty

6.1. The Authority's policy for imposing a financial penalty is set out in Chapter 6 of DEPP. The Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5B sets out the details of the five-step framework that applies in respect of financial penalties imposed on individuals in non-market abuse cases.

Step 1: disgorgement

6.2. Pursuant to DEPP 6.5B.1G, at Step 1 the Authority seeks to deprive an individual of the financial benefit derived directly from the breach where it is practicable to quantify this.

6.3. The Authority has not identified any financial benefit that Mr Stephen derived directly from the breach.

6.4. Step 1 is therefore £0.

Step 2: the seriousness of the breach

6.5. Pursuant to DEPP 6.5B.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breach. That figure is based on a percentage of the individual's relevant income. The individual's relevant income is the gross amount of all benefits received by the individual from the employment in connection with which the breach occurred, and for the period of the breach.

6.6. The period of Mr Stephen's breaches of Statements of Principle 1 and 6 was from 3 January 2018 to 2 August 2019. The Authority considers Mr Stephen's relevant income for this period to be £173,781.

6.7. In deciding on the percentage of the relevant income that forms the basis of the Step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 40%. This 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 individuals in non-market abuse cases there are the following five levels:

Level 1 – 0%

Level 2 – 10%

Level 3 – 20%

Level 4 – 30%

Level 5 – 40%

6.8. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, and whether it was committed deliberately or recklessly.

6.9. DEPP 6.5B.2G(12) lists factors likely to be considered 'level 4 or 5 factors'. Of these, the Authority considers the following factors to be relevant:

1) the breaches caused a significant loss to individual consumers (DEPP 6.5B.2G (12)(a));

2) Mr Stephen failed to act with integrity (DEPP 6.5B.2G(12)(d));

3) as an experienced individual in a senior management position, Mr Stephen abused a position of trust, and failed to put the customer at the heart of the decisions made, thus causing risk of loss to a large number of consumers (DEPP 6.5B.2G (12)(e)); and

4) the breach described in paragraphs 5.3 to 5.5 was committed recklessly (DEPP 6.5B.2G (12)(g)).

6.10. DEPP 6.5B.2G(13) lists factors likely to be considered 'level 1 or 2 or 3' factors. Of these, the Authority considers the following factor to be relevant:

1) some of Mr Stephen's breaches were committed negligently.

6.11. Taking all of these factors into account, the Authority considers the seriousness of the breaches to be level 4 and so the Step 2 figure is 30% of £173,781.

6.12. Step 2 is therefore £52,134.

Step 3: mitigating and aggravating factors

6.13. Pursuant to DEPP 6.5B.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.

6.14. The Authority has considered whether any of the mitigating or aggravating factors listed in DEPP 6.5B.3G, or any other such factors, apply in this case and has concluded that none applies to a material extent, such that the penalty ought to be increased or decreased.

6.15. Step 3 is therefore £52,134.

Step 4: adjustment for deterrence

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

6.17. The Authority considers that the Step 3 figure of £52,134 represents a sufficient deterrent to Mr Stephen, and so has not increased the penalty at Step 4.

6.18. Step 4 is therefore £52,134.

Step 5: settlement discount

6.19. The Authority and Mr Stephen have not reached an agreement to settle and so no discount applies to the Step 4 figure. Pursuant to DEPP 6.5B.5G, if the Authority and the individual 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 individual reached agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.

6.20. Step 5 is therefore £52,100 (rounded down to the nearest £100).

Penalty

6.21. The Authority has therefore decided to impose a total financial penalty of £52,100 on Mr Stephen for breaching Statements of Principle 1 and 6.

Prohibition Order

6.22. The Authority has the power to prohibit individuals under section 56 of the Act. The Authority has had regard to the guidance in Chapter 9 of the Enforcement Guide in considering whether Mr Stephen should be prohibited and the nature of any such prohibition. The relevant provisions of the Enforcement Guide are set out in Annex A to this Notice. In particular, the Authority has been mindful of the following:

a. whether the individual is fit and proper to perform functions in related to regulated activities;

b. whether, and to what extent, the approved person has failed to comply with the Statements of Principle issued by the Authority with respect to the conduct of approved persons;

c. the relevance and materiality of any matters indicating unfitness;

d. the particular controlled function the approved person was performing, the nature and activities of the firm concerned and the markets in which he operates; and

e. the severity of the risk which the individual poses to consumers and to confidence in the financial system.

6.23. Given the nature and seriousness of the failures set out above, Mr Stephen's conduct demonstrated a lack of integrity and competence such that he is not a fit and proper person to perform any senior management function and any significant influence function in relation to any regulated activities carried on by any authorised or exempt person, or exempt professional firm. The Authority considers that, in the interests of consumer protection, and in order to maintain market confidence, it is appropriate and proportionate in all the circumstances to impose on Mr Stephen the Prohibition Order in the terms set out above.

7. REPRESENTATIONS

7.1 Annex B contains a brief summary of the key representations made by Mr Stephen in response to the Warning Notice and how they have been dealt with. In making the decision which gave rise to the obligation to give this Notice, the Authority has taken into account all of the representations that it received on the Warning Notice, whether or not set out in Annex B.

8. PROCEDURAL MATTERS

8.1. This Notice is given to Mr Stephen under sections 57 and 67 of the Act and in accordance with section 388 of the Act.

8.2. The following statutory rights are important.

Decision maker

8.3. The decision which gave rise to the obligation to give this Notice was made by the RDC. The RDC is a committee of the Authority which takes certain decisions on behalf of the Authority. The members of the RDC are separate to the Authority staff involved in conducting investigations and recommending action against firms and individuals. Further information about the RDC can be found on the Authority's website:

https://www.fca.org.uk/about/committees/regulatory-decisions-committee-rdc

The Tribunal

8.4. Mr Stephen has the right to refer the matter to which this Notice relates to the Tribunal. Under paragraph 2(2) of Schedule 3 of the Tribunal Procedure (Upper Tribunal) Rules 2008, Mr Stephen has 28 days from the date on which this Notice is given to him to refer the matter to the Tribunal. A reference to the Tribunal is made by way of a signed reference notice (Form FTC3) filed with a copy of this Notice. The Tribunal's contact details are: Upper Tribunal, Tax and Chancery Chamber, Fifth Floor, Rolls Building, Fetter Lane, London EC4A 1NL (tel: 020 7612 9730; email: fs@hmcts.gsi.gov.uk).

8.5. Further information on the Tribunal, including guidance and the relevant forms to complete, can be found on the HM Courts and Tribunal Service website:

http://www.justice.gov.uk/forms/hmcts/tax-and-chancery-upper-tribunal

8.6. A copy of Form FTC3 must also be sent to the Authority at the same time as filing a reference with the Tribunal. A copy should be sent to Mark Lewis at the Financial Conduct Authority, 12 Endeavour Square, London E20 1JN.

8.7. Once any such referral is determined by the Tribunal and subject to that determination, or if the matter has not been referred to the Tribunal, the Authority will issue a final notice about the implementation of that decision.

Access to evidence

8.8. Section 394 of the Act applies to this Notice.

8.9. The person to whom this Notice is given has the right to access:

(1) the material upon which the Authority has relied in deciding to give this Notice; and

(2) the secondary material which, in the opinion of the Authority, might undermine that decision.

Third party rights

8.10. A copy of this Notice is being given to Stuart Anderson as a third party identified in the reasons above and to whom in the opinion of the Authority the matter to which those reasons relate is prejudicial. Mr Anderson has similar rights to those mentioned in paragraphs 8.4 and 8.9 above, in relation to the matter which identifies him.

Confidentiality and publicity

8.11. This Notice may contain confidential information and should not be disclosed to a third party (except for the purpose of obtaining advice on its contents). In accordance with section 391 of the Act, a person to whom this Notice is given or copied may not publish the Notice or any details concerning it unless the Authority has published the Notice or those details.

8.12. However, the Authority must publish such information about the matter to which a Decision Notice or Final Notice relates as it considers appropriate. The persons to whom this Notice is given or copied should therefore be aware that the facts and matters contained in this Notice may be made public.

Authority contacts

8.13. For more information concerning this matter generally, contact Mark Lewis at the Authority (direct line: 020 7066 8442 / email: mark.lewis2@fca.org.uk).

Tim Parkes
Chairman, Regulatory Decisions Committee

ANNEX A

RELEVANT STATUTORY AND REGULATORY PROVISIONS

1. RELEVANT STATUTORY PROVISIONS

1.1. The Authority's statutory objectives, set out in section 1B(3) of the Act, include the operational objective of securing an appropriate degree of protection for consumers (section 1C).

1.2. Section 66 of the Act provides that the Authority may take action against a person if it appears to the Authority that he is guilty of misconduct and the Authority is satisfied that it is appropriate in all the circumstances to take action against him. A person is guilty of misconduct if, while an approved person, he has failed to comply with a statement of principle issued under section 64A of the Act, or has been knowingly concerned in a contravention by a relevant authorised person of a relevant requirement imposed on that authorised person.

1.3. Section 56 of the Act provides that the Authority may make an order prohibiting an individual from performing a specified function, any function falling within a specified description or any function, if it appears to the Authority that that individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person, exempt person or a person to whom, as a result of Part 20, the general prohibition does not apply in relation to that activity. Such an order may relate to a specified regulated activity, any regulated activity falling within a specified description, or all regulated activities.

2. RELEVANT REGULATORY PROVISIONS

Statements of Principle and Code of Practice for Approval Persons

2.1. The Authority's Statements of Principle and Code of Practice for Approved Persons ("APER") have been issued under section 64A of the Act.

2.2. During the Relevant Period, Statement of Principle 1 stated:

"An approved person must act with integrity in carrying out his accountable functions."

2.3. During the Relevant Period, Statement of Principle 6 stated:

"An approved person performing an accountable higher management function must exercise due skill, care and diligence in managing the business of the firm for which they are responsible in their accountable function."

2.4. 'Accountable functions' include controlled functions and any other functions performed by an approved person in relation to the carrying on of a regulated activity by the authorised person to which the approval relates.

2.5. APER sets out descriptions of conduct which, in the opinion of the Authority, does not comply with a Statement of Principle. It also sets out factors which, in the Authority's opinion, are to be taken into account in determining whether an approved person's conduct complies with a Statement of Principle.

The Fit and Proper Test for Approved Persons

2.6. The part of the Authority's Handbook entitled *"The Fit and Proper Test for Approved Persons"* ("FIT") sets out the criteria that the Authority will consider when assessing the fitness and propriety of a candidate for a controlled function. FIT is also relevant in assessing the continuing fitness and propriety of an approved person.

2.7. FIT 1.3.1G states that the Authority will have regard to a number of factors when assessing the fitness and propriety of a person. The most important considerations will be the person's honesty, integrity and reputation, competence and capability and financial soundness.

The Authority's policy for exercising its power to make a prohibition order

2.8. The Authority's policy in relation to prohibition orders is set out in Chapter 9 of the Enforcement Guide ("EG").

2.9. EG 9.1 states that the Authority may exercise this power where it considers that, to achieve any of its regulatory objectives, it is appropriate either to prevent an individual from performing any functions in relation to regulated activities or to restrict the functions which he may perform.

Conduct of Business Sourcebook

2.10. The Authority's rules and guidance for Conduct of Business are set out in COBS. The rules in COBS relevant to this Notice are 2.1.1R, 2.3A.15R, 11.2A.2R, 16.2.3R, 16.3.2R(1), 16A.4.1 60(2) and 16 Annex 1R.

Senior Management Arrangements, Systems and Controls Sourcebook

2.11. The Authority's rules and guidance for senior management arrangements, systems and controls are set out in SYSC. The rules in SYSC relevant to this notice are 10.1.3R, 10.1.4R, 10.1.6R, 10.1.7R, 10.1.8R.

Product Intervention and Product Governance Sourcebook

2.12. The Authority's rules and guidance for Product Intervention and Product Governance are set out in PROD. The rules and guidance in PROD relevant to this notice are 3.3.1R, 3.3.3R and 3.3.15R(3).

Decision Procedure and Penalties Manual

2.13. Chapter 6 of DEPP sets out the Authority's statement of policy with respect to the imposition and amount of financial penalties under the Act.

ANNEX B

David Stephen's Representations

1. A summary of the key representations made by Mr Stephen, and of the Authority's conclusions in respect of them (in bold type), is set out below.

The reality of Mr Stephen's role and responsibilities

2. Much of the misconduct alleged by the Authority arose as a result of: (1) commercial decisions made by Mr Virk; (2) the secret commission arrangements that Mr Virk entered into with various third parties; and (3) the close relationship Mr Virk had with Mr Anderson. Mr Virk benefitted financially from these arrangements/relationships. Mr Virk concealed from Mr Stephen the fact of the relationships, the commercial arrangements and the benefits he received, and Mr Stephen was an unknowing bystander to Mr Virk's deception. Mr Stephen, as the Compliance Officer, did not, and was not in a position to, take or influence the commercial decisions made by Mr Virk. He was not fully sighted on the commercial agreements and the underlying commercial rationale behind them.

3. Mr Virk made the decisions to enter into the commercial arrangements and it was the Investment Committee that had the responsibility to make decisions as to what products to invest in, and to carry out the necessary due diligence. Mr Stephen was not involved with this process.

4. Mr Stephen was not a director and did not sit on either of the two key internal committees, namely, the Board of Directors and/or the Investment Committee. He only attended such meetings at the request of the directors to discuss any Compliance matters that they made him aware of. As part of Mr Stephen's role, as Head of Compliance, from time to time he challenged and pushed back on proposals made by SVS's senior management team.

5. **The Authority's expectation of a holder of a CF10 (Compliance Oversight) function during the Relevant Period was set out in SUP 10A.7.8R[1] (with reference to SYSC 3.2.8R[2]), namely as a director or senior manager to have responsibility for oversight of the firm's compliance and to report to the governing body in respect of that responsibility.**

6. **By virtue of SYSC 6.1.2R and 6.1.3R, the compliance function was required to operate independently and to monitor and, on a regular basis, to assess the adequacy and effectiveness of the measures and procedures put in place by a firm to detect any risk of failures by the firm to comply with its obligations under the regulatory system, and the actions taken to address any deficiencies in the firm's compliance with its obligations.**

7. **In the Authority's view, it was not open to Mr Stephen, as the firm's CF10 and Head of Compliance, to disregard his responsibility for oversight of the adequacy and effectiveness of the measures and procedures with respect to**

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[1] https://www.handbook.fca.org.uk/handbook/SUP/10A/?date=03-01-2018&timeline=True&view=chapter
[2] https://www.handbook.fca.org.uk/handbook/SYSC/3/2.html?date=2018-01-03#D33

important activities of the firm, namely its discretionary fund management business, on the basis that this was the responsibility of others. The Authority expects a CF10 to be proactive in the fulfilment of their responsibility.

8. **Whether Mr Stephen: (i) knew of Mr Virk's commercial arrangements; or (ii) challenged SVS's senior management team on certain proposals, does not affect Mr Stephen's culpability for the particular matters set out in the Notice, because these are matters which he should have made himself aware of through diligent enquiry, given the proactivity expected when discharging a CF10 role.**

Decision to introduce a mark-down on fixed income disinvestments

9. As was stated in the Model Portfolio brochures, all investments including fixed income bonds were subject to a dealing fee when they were bought or sold. It had been open to SVS to charge such dealing fees on all investment transactions within the Model Portfolios from the outset of the Model Portfolios in January 2016. Before November 2018, if a client wanted to disinvest, it was always open to SVS to buy the bonds as principal, or to totally disinvest in the marketplace, or to sell to another buyer on a matched principal basis. This had been disclosed to clients in the Model Portfolio brochure and terms and conditions, together with the expectation that the investments would be held to maturity. The brochure specifically stated *"…and if they are sold before maturity you may receive less back than your original investment…".*

10. However, the SVS Board realised that SVS had inadvertently been buying disinvesting clients' investments from them at par (i.e. the same price at which the clients had bought them). This was never the Board's intention and had been an oversight. In October 2018, the disinvestment process was reviewed, and whilst the suggestion of an exit charge was not adopted, SVS favoured an approach whereby it reverted to accepted market practice, namely that if clients wanted to disinvest, they would disinvest at the then market price for the bond and in accordance with the "best execution" rules. Applicable dealing fees and associated disinvestment spreads were also applied to all disinvestment requests, whether the underlying investments were equities or fixed income products.

11. Mr Stephen recalls being told that at around this time Mr Virk spoke to Mr Anderson and was informed by him that the bonds issued by CFBL would trade in the secondary market at a discount of 30-50%. Hence, Mr Stephen considered that, in accordance with the "best execution" rules, SVS could have disinvested the investors at this secondary market price; however, instead a commercial decision was taken by the directors, led by Mr Virk, that disinvestment would take place at a cost of 10% to the client. This figure was therefore not arbitrary, and nor was it a commission - it related to the "best execution rules" and a desire by SVS to be fair to the disinvesting clients. Had SVS not offered the 10% market spread, the only market spread available to these disinvesting clients would have been the 30-50% suggested by Mr Anderson, resulting in a greater cost to them. The 10% market spread was therefore more advantageous to clients than disinvesting them at the secondary market price.

12. The reason for introducing the 10% spread was, therefore, to bring an end to the previous status quo which had been overly generous to investors by virtue of SVS's oversight, and had inadvertently continued for some time, whilst striking a fair

balance. IFAs/SIPP Trustees were provided with disinvestment spreadsheets which made it clear that a 10% spread had been applied to fixed income investments. All disinvestments were carried out in line with the Model Portfolios' Terms and Conditions, as detailed in the client literature and agreements. The 10% spread simply brought SVS into line with accepted market practice. SVS did not impose an exit charge on investors for disinvesting.

13. Mr Stephen considers that the assertion that he "*actively supported*" the implementation of the decision, mischaracterises what happened: it was a matter for the Board of SVS what it wished to do from a commercial perspective. However, it was Mr Stephen's role to assess whether it was permissible from a regulatory/compliance perspective. Mr Stephen's view was that it was permissible and was in accordance with the "best execution" rules. In so far as Mr Stephen supported the Board's decision, he did so from a compliance perspective and did not actively support the decision or its implementation.

14. Mr Stephen accepts that concerns were expressed about the suggested disinvestment process, and amongst other things, the rationale for the 10% spread. Mr Stephen's view, shared by the Board, was that these concerns were an attempt by certain employees to re-visit decisions which had already been made by the Board. As the material facts had not changed, in Mr Stephen's view there was little point in endlessly debating the same issue. He did not ignore these internal concerns. No formal complaints were received by Mr Stephen or SVS about the disinvestment process.

15. Mr Stephen honestly believed that the 10% market spread was in accordance with the best execution requirements as he understood them at the time. He was not reckless. He understood that the spread was apparent from the disinvestment spreadsheet statements sent to the IFAs, SIPP providers and clients by SVS.

16. Mr Stephen did not believe, at the time, that the 10% market spread was intended to generate more income for SVS. The Model Portfolio business only accounted for 25% of SVS's total, regulated business in any event. Although a consequence of the application of the 10% spread may have been that SVS did obtain additional revenue, this was not the driver behind adopting it; rather, it was to bring SVS in line with standard market practice on disinvestments and, in doing so, to achieve a better outcome for disinvesting clients than they would have otherwise been offered in the secondary market.

17. In acting as principal to facilitate these disinvestments and to provide liquidity, SVS bought the fixed income investments onto its principal book. Mr Stephen notes that there has been no investigation by the Authority, nor is there evidence, as to what happened to these fixed income investments, once they were bought onto SVS's principal book. Instead, there has simply been an assertion by the Authority that SVS immediately sold them to other SVS Model Portfolio investors at par and took no market risk in doing so. Mr Stephen notes Mr Virk's statement to the Authority that there were some instances, where some of these investments remained on the SVS principal trading book for up to six months. On that basis, SVS was taking market risk and tying up its own capital.

18. **If SVS's clients held their interest in the fixed income investments until maturity, they could have expected to receive back 100% of the price which they had paid for that interest, unless the bond issuer had become insolvent**

in the meantime. Whilst the fixed income investments were being held, clients were also entitled to their share of the regular coupon payments which were made by the product issuers. Furthermore, during that period SVS accounted to clients for the value of the fixed income investments at par (i.e. 100% their issue price). At some point prior to 2 November 2018, it was suggested within SVS that clients who sought to disinvest should no longer receive the full value of the fraction of the fixed interest investments currently attributed to them. The scheme devised by SVS was for it, as principal, to acquire such investments from the disinvesting clients at 90% of their par value and then allocate them to other clients invested in the Model Portfolios at 100%. The person who conducted the trades in question for SVS stated to Mr Stephen and others on 5 December 2018 that: *"The models will purchase via CROSS from disinvesting clients at MID [mid-market price]. The client will be charged the flat 10% thereafter as a contract charge. This has the net effect of the firm making the 10% cut on price."*

19. **The fixed income investments within the Model Portfolios were from different bond programmes, each of which had different maturity dates and preference share issues. Accordingly, there was no single maturity date for the Model Portfolios, at which a disinvestment mark-down could be avoided. Although investors were informed that the fixed income investments should be held for five years, they were entitled to realise their investments at any time in accordance with SVS's Model Portfolio terms and conditions of business. Since the majority of the £69.6 million invested in the Model Portfolios represented money invested on behalf of SVS's clients for the purpose of funding their pensions the Authority considers that Mr Virk must have known that certain of those clients were likely to wish to realise their investments for retirement, by disinvesting, before some or all of those maturity dates. This meant that, sooner or later, certain of the investors would incur the 10% disinvestment mark-down. In practice, the revenue which accrued to SVS from the 10% mark-down totalled £359,800.**

20. **Mr Stephen asserts that the only other option available to investors would have been for the investments to be sold in the secondary market or for SVS to buy them at around 50-70% of their par value, reflecting what Mr Anderson had apparently said was the likely secondary market price for CFBL's Bonds. However, there is no evidence that Mr Stephen or SVS conducted any investigation of the secondary market price for the fixed income investments held in the Model Portfolios; rather, it appears that Mr Stephen relied on what he understood Mr Anderson had said to Mr Virk.**

21. **Furthermore, prior to the adoption by SVS of the mark-down, SVS had itself made a market for the fixed income products by routinely using the Model Portfolios to purchase them from disinvesting clients at par value (100%). Accordingly, the Authority considers that Mr Stephen is wrong to suggest that the only other option available to disinvesting investors would have been a sale at a discount of about 30-50%; the investments could have been purchased by SVS's Model Portfolios at par, as had previously been the case.**

22. **The Authority has not seen any evidence that SVS was holding the disinvested investments on its principal book at all, let alone for up to six months, as asserted by Mr Virk to the Authority, and the evidence referred to**

in paragraph 17 suggests the contrary. The Authority concludes that in reality there was no market risk for SVS, and that the Authority considers that the 10% mark-down was not a "best execution" market spread; it simply constituted a profit for SVS. As such, the disinvestment mark-down scheme was contrary to investors' best interests.

23. **The Model Portfolio brochures and terms of business allowed principal trading by SVS but they only referred to SVS '*selling shares that we own*'. There was no reference to SVS buying fixed income investments from disinvesting customers at 90% of par value and selling them to the Model Portfolios at 100%. Clients were, in effect, locked into investments which, from around November 2018 (but not before) they could not exit without the fixed interest portion of their investments being marked down by 10%. This also meant that the valuation reports sent to clients (which continued to show their fixed income investments at par) represented a higher value for them than on Mr Stephen's case the clients could hope to obtain on disinvestment.**

24. **Even if clients had been informed of the 10% mark-down before they disinvested (which they were not), by that stage they had no opportunity to avoid the mark-down to which they had not agreed. The disclosure of the mark-down should have been made by SVS in the Model Portfolio brochures and/or Terms of Business, if it was to be imposed at all.**

25. **The only evidence of *any* disclosure of which the Authority is aware is in a spreadsheet sent to an IFA, not to clients. It did not state that SVS acted as principal in the disinvestment process and therefore did not disclose SVS's role in generating a profit for itself of 10%. Even if disinvestment contract notes disclosed the figure for the charge (and thus profit) made by SVS, that disclosure was too late. SVS saw an opportunity to make a profit of 10% from disinvesting clients without fairly disclosing that profit to them at the appropriate time, and it took that opportunity with Mr Stephen's sign-off and support.**

26. **Amongst the concerns about this proposal one was raised directly with Mr Stephen by a senior member of staff (summarised at paragraph 4.43 of this Notice), who, amongst other things, asked Mr Stephen the question: "*should we really be trying to profit from it [the potential cost of disinvestment] and on a level which would be much higher than any potential exit charge?*". The Authority expects any CF10 and Head of Compliance, faced with a senior member of staff repeatedly raising concerns about fairness to customers, to take those concerns seriously. Instead, Mr Stephen ignored and dismissed them.**

27. **The Authority considers that Mr Stephen acted recklessly in respect of the concerns raised, including by the senior member of staff concerned, that the charge was not fair to customers. Mr Stephen was aware of the risk of unfairness, since it had been raised with him directly. By ignoring and dismissing those concerns, Mr Stephen exposed SVS's clients to the risk of harm.**

Acceptance of lower risk customers for the Model Portfolio

28. Mr Stephen considers that SVS was a product manufacturer, not a distributor, within the meaning of the PROD rules; it set up a portfolio in which investors could invest through their IFAs, and at no time was there any direct selling by SVS to these IFAs' clients. However, and in any event, SVS and Mr Stephen took adequate steps to ensure that it was only investors with a high-risk profile, who invested in the Model Portfolio.

29. It was not improper for SVS only to carry out an appropriateness assessment; nor was it wrong for SVS and Mr Stephen to rely on the IFAs to carry out suitability assessments. Mr Stephen considers that the Authority's incorrect view is based on the flawed premise that SVS was a product distributor. SVS was not a product distributor and therefore not subject to PROD 3.3.15R(3)[3]. It was the responsibility of the IFAs to check the suitability of these investments for their retail clients before advising them to invest.

30. Mr Stephen reasonably expected the IFAs to carry out their regulatory and legal duties with due skill and care. The letters sent by IFAs to clients made it clear that the IFAs understood that they had the responsibility to assess the suitability of the investments for the client which would cover, amongst other things, how the Model Portfolio would fit into a client's overall investment objectives(s), and that as a matter of fact, they had done so. If IFAs had not executed their duties properly at the time, Mr Stephen considers that this would not invalidate the reasonableness of SVS's position at the time.

31. SVS provided the IFAs with, amongst other things, the following information: (1) a copy of the Model Portfolio Brochure: this provided an explanation of the Model Portfolios and expressly identified that the Model Portfolios were *'high-risk'*; and (2) other documentary material, as appropriate. The IFAs were also aware of the fees charged by SVS and would conduct their own due diligence on the Model Portfolios and the assets contained within them. SVS employees would also visit the IFAs and explain how the Model Portfolios operated, the assets within them, and the fee structure. Mr Stephen considers that IFAs were aware, or ought reasonably to have been aware, of how the Model Portfolios operated and the assets within them.

32. In addition to the obligation on the IFAs to carry out suitability assessments, SVS would itself carry out an appropriateness assessment, verbally over the telephone, to ensure that, amongst other things, the clients understood the risks involved. SVS checked the information the IFA had provided to them was accurate. This was to review the applications from an appropriateness point of view, and to seek to ensure

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[3] PROD 3.3.15R:
(1) Distributors must have in place adequate product governance arrangements to ensure that: (a) the financial instruments and investment services they intend to distribute are compatible with the needs, characteristics and objectives of the identified target market; and (b) the intended distribution strategy is consistent with the identified target market.
(2) Distributors must appropriately identify and assess the circumstances and needs of the clients they intend to focus on to ensure that their clients' interests are not compromised as a result of commercial or funding pressures.
(3) Distributors must identify any groups of end clients for whose needs, characteristics and objectives the financial instrument or investment service is not compatible.

that no investment was accepted by SVS from customers for whom the Model Portfolios had a higher risk than they were willing or able to bear. The Model Portfolio brochure detailed the respective responsibilities of the IFAs and SVS, when a customer account was opened.

33. A script of questions was prepared for the SVS employee so that the correct questions were asked, and on a number of occasions SVS rejected investors on the grounds that SVS had formed a view that the investor did not properly understand the risks. A number of complaints were made by investors to the Financial Ombudsman Service, but all were dismissed and none upheld, thereby demonstrating that SVS had at all times acted fairly and appropriately with investors.

34. Mr Stephen considers that SVS acted in accordance with its regulatory obligation to carry out an appropriateness assessment. Mr Stephen took reasonable steps to ensure that it was only investors with a high-risk profile, who invested in the Model Portfolios.

35. **Mr Stephen's argument, that SVS's services were that of a product "*manufacturer*", rather than a "*distributor*", for the purposes of PROD 3, is incorrect. A "*distributor*" is defined in the Glossary to the Handbook, in relation to PROD 3, as: "*a firm which offers, recommends or sells investments or provides investment services to clients*"[4]. "*Investment service*" is defined as any of a list of services, including "*(b) execution of orders on behalf of clients*" and "(d) *portfolio management*"[5]. '*Portfolio management*' is defined as "*managing portfolios in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments*"[6]. SVS bought investments for each client, in line with the relevant Model Portfolio. SVS therefore managed investments on behalf of each investor.**

36. **Purchases of investments were made on a pooled basis, and SVS would make large investments on behalf of the Model Portfolios, with each investor treated as holding their share of the investments. Even though investments were purchased en bloc, they were attributable to each client (as shown in the clients' statements) and were purchased and sold on a client-by-client basis. The Authority considers that SVS, therefore, provided the investment service of portfolio management, and fell within the definition of "*distributor*".**

37. **A "*manufacturer*" is defined in the Glossary, in relation to PROD 3, as "*a firm which creates, develops, issues, and/or designs investments, including when advising corporate issuers on the launch of new investments*"[7]. Clients were not buying a unit in a SVS Model Portfolio. SVS was not selling a unit in a SVS Model Portfolio. If SVS had been doing so, then the Authority considers that**

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[4] https://www.handbook.fca.org.uk/handbook/glossary/?starts-with=D
[5] https://www.handbook.fca.org.uk/handbook/glossary/?starts-with=I
[6] https://www.handbook.fca.org.uk/handbook/glossary/?starts-with=P
[7] https://www.handbook.fca.org.uk/handbook/glossary/?starts-with=M

it would almost certainly have been operating a collective investment scheme[8], a permission that SVS did not have.

38. **Accordingly, the Model Portfolios were not themselves an "*investment*" and SVS was not a "*manufacturer*". It was a "*distributor*".**

39. **The Model Portfolios were high-risk. The majority of the £69.6 million invested through SVS represented money which was to fund clients' pensions. Mr Stephen appears to accept that SVS did not, as a matter of course, seek to ensure that its service was compatible with client's needs, characteristics and objectives, beyond the appropriateness assessment that it undertook. This was a breach of PROD 3.3.15R[9]. If it had done so, it would have ascertained that the high-risk Model Portfolios, and SVS's discretionary management service, were not compatible with the risk appetites of many customers. The lack of proper compliance oversight contributed to retail clients investing in the products: had proper checks on customers' risk appetites been carried out by SVS, the Authority considers that certain of SVS's clients would not have invested in the Model Portfolios.**

40. **The Authority considers that Mr Stephen, as CF10 and the firm's Head of Compliance, failed to take reasonable steps to ensure that it was only investors with a high-risk profile, who invested in the Model Portfolios. As SVS was a distributor, and therefore PROD 3.3.15R directly applied to it, it was inappropriate for Mr Stephen to rely on the IFA for compliance with this rule.**

Inducements

41. SVS did not operate a business model that relied upon financial incentives to market its discretionary managed Model Portfolios to retail customers. There is nothing wrong, in principle, with a regulated entity having in place commission arrangements as long as, amongst other things, any duties to the investor are not compromised. In any event, the Model Portfolio, being at 25%, was a minor component of SVS's overall business.

42. SVS's receipt of the payments for the provision of corporate services to bond providers did not constitute inducements. It is not correct to assert that SVS took up to 12% of its customers' funds for commission in respect of fixed income products. Customer funds were not used to pay these corporate consultancy fees that the bond providers had agreed to pay SVS from their own funds.

43. The level of commissions received by SVS did not represent a level of inducement that put at risk SVS's independence and compromised its ability to act in the best interests of its customers. The governance system within SVS, which Mr Stephen notes has not been criticised by the Authority, ensured that the decisions as to which assets to invest in were taken by the Investment Committee, which made its decisions independently. Mr Stephen was not, in any event, involved in this decision making.

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[8] Establishing, operating or winding up a collective investment scheme is a specified kind of activity under Article 51ZE of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.

[9] ibid

44. Mr Stephen denies that SVS was not compliant with the rules relating to inducements from 3 January 2018 onwards. Moreover, SVS and Mr Stephen obtained legal advice from a large City firm of solicitors, and was assured that the commission received by SVS, and the commission paid to introducers, were compliant with relevant rules. Mr Stephen considers that he took reasonable steps to ensure SVS remained compliant after 3 January 2018, the date when COBS 2.3A.15R came into force, by seeking legal advice on the issue.

45. **SVS invested its clients' funds into fixed income investments in respect of which SVS received large commissions. SVS then paid commissions of 7% to 9% to unauthorised introducers, some of which were owned by the same individual as the IFA advising SVS's clients. The risk of an introducer's interests affecting the independence of the IFA's advice is obvious. This was the message of the Authority's guidance in August 2016, which included the warning that: "*Many authorised firms receive customer introductions from introducers. We are very concerned at the increase we have seen in cases in which the introducer has an inappropriate influence on how the authorised firm carries out its business, in particular where the introducer influences the final investment choice*"[10].**

46. **The Authority considers that the clear purpose of the marketing agreements (referred to in paragraph 4.28 of the Notice) was that introducers would only receive commission, if clients invested through the Model Portfolios. SVS ought to have been concerned about the commissions influencing advice from the IFAs, and whether their duties to SVS's clients were compromised.**

47. **Mr Stephen was aware of the commission-driven commercial arrangements with the fixed income investment providers, as well as the payments to unauthorised introducers. Indeed, he specifically highlighted to other directors the Authority's concerns about such introducers, yet he failed to act in respect of the risk that such introducers would influence the advice given by supposedly disinterested IFAs to SVS's clients. Mr Stephen's knowledge of and involvement in these arrangements and failure to act exposed SVS's clients to the risk of harm.**

48. **The absence of criticism of the governance procedures in this Notice should not be taken to mean that the Authority is content with the governance systems within SVS in relation to its investment decisions. In particular, the Authority considers that Mr Virk influenced the Model Portfolio investment decisions, and that those decisions were made before the Investment Committee considered the relevant investments.**

[10] https://www.fca.org.uk/news/news-stories/investment-advisers-responsibilities-accepting-business-unauthorised-introducers-lead-generators

49. **COBS 2.3A.15R[11] came into force on 3 January 2018 and provided that discretionary managers must not accept fees or commissions from any third party in relation to the provision of the relevant service to the client. Mr Stephen knew that commissions were received. Accordingly, he knew the true factual position. The level of commissions received by SVS were not minor, nor non-monetary, and nor could they be said to have been paid for third party research.**

50. **If legal advice was provided that the commissions were acceptable, the Authority considers that it could only have been reasonably provided on an erroneous understanding of the factual position. Mr Stephen has not explained the nature of that advice or how SVS's receipt of commissions could have complied with the relevant rules.**

51. **In addition, the Authority refers to the following comments in *Financial Conduct Authority v Forster and others*[12]: *"However, it is equally important to emphasise that an independent legal opinion is not a get-out-of-jail-free card. The term "a legal opinion" covers a bewildering array of different forms of advice: some absolute; some conditional; some tentative; and all based on a series of factual assumptions whose accuracy is generally outside the scope of knowledge of the legal advisor. There can be no hard rule as to the legal effect of "a legal opinion" – everything depends on the circumstances".***

52. **Whatever legal advice SVS and Mr Stephen received, the Authority considers that it cannot change the factual position, which was within Mr Stephen's knowledge. Accordingly, the Authority considers that, during the Relevant Period, the receipt of commission by SVS was in direct contravention of COBS 2.3A.15R and that Mr Stephen did not take reasonable steps to ensure that SVS was compliant with the rules relating to inducements.**

Fairness and disclosure

53. Mr Stephen considers that an adequate disclosure exercise has not been carried out by the Authority. This has created a situation whereby crucial evidence relating to key events, is missing.

54. Had this information been disclosed, it would have revealed the internal challenges that Mr Stephen faced, as well as his efforts to try and ensure that the SVS directors and the Model Portfolio managers and team acted in a compliant manner. Mr Stephen was denied access to all his SVS emails and SVS records. This lack of access and lack of adequate disclosure has resulted in Mr Stephen being severely hampered in his ability to properly defend himself.

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[11] COBS 2.3A.15R(1) This rule applies where a firm provides a retail client in the United Kingdom with… (c) portfolio management services.
(2) The firm must not accept any fees, commission, monetary or non-monetary benefits which are paid or provided by … any third party … in relation to the provision of the relevant service to the client. …
(3) Paragraph (2) does not apply to:
(a) acceptable minor non-monetary benefits (see COBS 2.3A.19R); (b) third party research received in accordance with COBS 2.3B (see COBS 2.3B.3R).

[12] Financial Conduct Authority v Forster and others [2023] EWHC 1973 (Ch) at paragraphs 248 and 249 https://www.bailii.org/ew/cases/EWHC/Ch/2023/1973.html

55. Mr Stephen points to a number of disclosure failures during the investigation including disclosure of relevant material subsequent to his oral representations meeting. The Tribunal has recently expressed concerns with the Authority's disclosure failures in *Seiler and others v Financial Conduct Authority*[13] and found that it could not be satisfied there were no other relevant documents that should have been disclosed. The same issues arise in Mr Stephen's case resulting in unfairness towards him.

56. **The Authority through the relevant team in the Enforcement and Market Oversight Division has responded to all the concerns related to disclosure which have been raised by Mr Stephen. The Authority's disclosure obligations, which apply to the giving of the Warning Notice and this Notice to Mr Stephen, are set out in section 394 of the Act. This requires the Authority[14] to allow the recipient of a specified statutory notice access to: (1) the material on which the Authority relied in taking the decision which gave rise to the obligation to give the notice; and (2) any secondary material which, in the Authority's opinion, might undermine that decision.**

57. **The Authority accepts there has, on occasion, been late disclosure, but it is satisfied, as at the date of this Notice, that there are no other relevant documents that should have been disclosed and does not consider that any unfairness has resulted to Mr Stephen as a result.**

<u>Sanction</u>

58. The financial penalty is disproportionate.

59. The concerns raised within the Notice focus entirely on one small part of SVS's business, namely the Model Portfolio (25% of SVS's total regulated business during the Relevant Period). In so doing, the Authority fails to understand, and therefore fails to take into account, that as the Compliance Officer, Mr Stephen was responsible for compliance matters across the whole of the business, which accounted for the vast majority (around 75%) of SVS's revenues. This creates a distorted view as to how Mr Stephen discharged his duties as the Compliance Officer. Even in relation to the Model Portfolios, the Financial Ombudsman Service did not uphold any of the complaints made during the Relevant Period.

60. As there is no criticism of Mr Stephen's conduct and performance in relation to his work regarding the remaining 75% of the SVS's regulated business, Mr Stephen considers that it is not fair and/or proportionate that no pro-rata adjustment has been applied to his relevant income figure for the calculation made at Step 2.

61. **The Authority has calculated the financial penalty by following the guidance on an individual's "*relevant income*" as set out in DEPP 6.5B.2G(1) and (3).**

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[13] Seiler and others v Financial Conduct Authority [2023] UKUT 00133 (TCC)
https://www.gov.uk/tax-and-chancery-tribunal-decisions/thomas-seiler-louise-whitestone-and-gustavo-raitzen-v-the-financial-conduct-authority-2023-ukut-00133-tcc

[14] Subject to statutory exceptions.

62. **"*Relevant income*" is the gross amount of all benefits received by the individual from the employment in connection with which the breach occurred (the "*relevant employment*"), and for the period of the breach. The guidance makes clear that the Authority recognises that "*in some cases an individual may be approved for only a small part of the work he carries out on a day-to-day basis. However, in these circumstances the Authority still considers it appropriate to base the relevant income figure on all of the benefit that an individual gains from the "relevant employment", even if their employment is not totally related to a controlled function".***

63. **The Authority considers that the same principle applies in Mr Stephen's case: it is appropriate to base the relevant income figure on all the benefit that Mr Stephen gained from his employment at SVS during the Relevant Period, even if the matters described within this Notice relate to the Model Portfolios only. Accordingly, the Authority considers that it is fair and proportionate not to make a pro-rata adjustment to his relevant income figure for the calculation made at Step 2.**