FINAL NOTICE

To: **Deloitte & Touche Wealth Management Limited**

Of: **Hill House**
1 Little New Street
London
EC4A 3TR

Date: **27 January 2004**

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("the FSA") gives Deloitte & Touche Wealth Management Limited ("DTWM") final notice about a requirement to pay a financial penalty

1 THE PENALTY

1.1 The FSA gave DTWM a Decision Notice dated 27 January 2004 which notified DTWM that, pursuant to section 206 of the Financial Services and Markets Act 2000 ("the Act"), the FSA had decided to impose a financial penalty on DTWM in the amount of £750,000 in respect of breaches of the Rules of the Personal Investment Authority ("PIA") including the Adopted FIMBRA Rules, and the Principles of the Securities and Investments Board ("the SIB Principles") in the period between 1997 and 2001 ("the relevant period").

1.2 DTWM has confirmed that it does not intend referring the matter to the Financial Services and Markets Tribunal.

1.3 Accordingly, for the reasons listed below and having agreed with DTWM the facts and matters relied upon, the FSA imposes a financial penalty of £750,000 on DTWM ("the Penalty").

2 RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES

2.1 Section 206 of the Act provides:

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

2.2 The Financial Services and Markets Act 2000 (Transitional Provisions and Savings)(Civil Remedies, Discipline, Criminal Offences etc)(No 2) Order 2001 ("the Pre-N2 Misconduct Order") provides, at Article 8(2), that the power conferred by Section 206 of the Act can be exercised by the FSA in respect of failures by a firm to comply with any of the provisions specified in Rule 1.3.1(6) of the Rules of the PIA ("PIA Rules") as if the firm had contravened a requirement imposed by the Act.

2.3 PIA Rule 1.3.1(6) provided that a PIA Member which failed to comply with PIA Rule 1.3.1(2) or any of the SIB Principles is liable to disciplinary action.

2.4 PIA Rule 1.3.1(2) provided that a PIA Member must obey the PIA Rules, which included the Adopted FIMBRA Rules and the SIB Principles.

2.5 PIA Rule 1.8.8(2)(d) provided that any manager appointed by the PIA Member to take day-to-day responsibility for the conduct of one or more advisers of the Member's relevant business must apply for individual registration with the PIA.

2.6 PIA Rule 1.8.8(5) provided that where the Member appointed or intended to appoint an individual to perform the functions of a registrable individual, the Member had to ensure that an individual did not begin to perform the functions of his new appointment until the Member received notice from the PIA that he had been entered in the Register of Individuals.

2.7 PIA Rule 1.8.9(2) provided that, with regard to a Member supporting an application by an individual for registration, the Member had to be satisfied on reasonable grounds that the applicant was fit and proper to be a registered individual.

2.8 PIA Rule 2.6.1(1) provided that a Member had to establish and implement a programme appropriate to its business and satisfactory to PIA for the training and supervising of its staff.

2.9 PIA Rule 5.1.1(1) provided that a Member had to keep records which were sufficient to show at any time that it had complied with the requirements of the Rule Book and had to establish procedures and controls to ensure that those records were made promptly and accurately and, where appropriate, brought up-to-date at regular and frequent intervals.

2.10 PIA Rule 7.2.1(1)(a) provided that a Member had to monitor adequately the conduct of its investment staff and other employees, with a view to ensuring compliance with the procedures which it had established in accordance with PIA Rule 7.1.2 and its own compliance with the PIA Rules and the SIB Principles.

2.11 PIA Rule 7.2.2 provided that:

i. where it appeared to the PIA that it was necessary or desirable in the interests of investors, the PIA could require a Member (or a class of Members) to carry out a review of any aspect of its investment business with a view to determining whether redress should be offered to any investor who had suffered loss or damage as a result of a failure by the Member to comply with its relevant duties;

ii. the PIA could prescribe the standards and a specification for the conduct of any such review; and

iii. a Member to whom any such requirement applied should take all reasonable steps to carry out a review of its investment business in accordance with such standards and specification as the PIA may prescribe.

2.12 Adopted FIMBRA Rule 29.5.1(1) provided that recommendations could only be made where there were good grounds for believing them to be suitable for the client in the light of any information given by the client and of any relevant facts about the client of which an adviser was, or ought to have been, aware.

SIB Principles

2.13 The SIB Principles were universal statements of standards expected of regulated firms and applied to PIA Members up to 30 November 2001.

2.14 SIB Principle 2 provided that a firm should act with due skill, care and diligence.

2.15 SIB Principle 9 provided that a firm should organise and control its internal affairs in a responsible manner and where the firm employed staff, should have adequate arrangements to ensure that they were suitable, adequately trained and properly supervised and that it had well-defined compliance procedures.

REASONS FOR THE ACTION

3 Summary of Conduct in Issue

3.1 On the basis of the Facts and Matters relied on, the FSA has decided to impose the penalty on DTWM in respect of breaches of the PIA Rules, Adopted FIMBRA Rule and SIB Principles specified in Section 2 arising from the structure and implementation of its compliance arrangements during the relevant period and the conduct of its Pensions Review.

3.2 By virtue of these matters DTWM has demonstrated regulatory failings which demand a substantial financial penalty. These failings are viewed by the FSA as particularly serious in light of the following factors:

i. the failings in DTWM's compliance arrangements, which were systemic and continued for a prolonged period of time, resulted from an approach to compliance adopted among DTWM's senior compliance management up to October 2000 which the FSA regards as wholly unacceptable. This approach proceeded on the basis that the PIA Rules relating to the documentation of

information from clients and the documentation of advice added no value to DTWM's business and were unnecessary;

ii. DTWM had been placed on notice on a number of occasions, in particular in a 1999 report from the PIA and by its own internal compliance reports in 2000 and 2001, that there were concerns relating to its compliance arrangements and the practices of its advisers. DTWM failed to pay sufficient attention to these warnings;

iii. the FSA considers that, taken together, these matters evidence that DTWM's approach to fundamental aspects of compliance up to October 2000 amounted to a disregard for the standards and requirements of the regulatory system, to the point that, had it not been for the decisive action (described in paragraph 3.3) which was taken after new management assumed control of DTWM, the FSA would have considered proposing to cancel DTWM's permission under Part IV of the Act to conduct regulated activities;

iv. DTWM's record keeping arrangements were so inadequate that they severely hindered DTWM's ability to conduct its Past Business Review ("PBR") in a timely manner. This was illustrated by the fact that in some 97% of all cases reviewed DTWM was unable to ascertain from its records whether advice given had been suitable or not and that meant that compensation which might have been due in respect of unsuitable advice was unacceptably delayed;

v. DTWM's Pensions Review failings could have been avoided as it had ready access to expertise that could readily have ensured that it was carried out effectively and in a timely manner. DTWM was owned by the UK Partnership of Deloitte & Touche ("Deloitte & Touche") and members of its senior management during the relevant period were partners of Deloitte & Touche, which included a substantial and highly regarded financial services advisory practice in this very area. Adequate resources were available to work on DTWM's Pensions Review but were deployed to work on the Pensions Reviews of chargeable outsourced client contracts;

vi. furthermore, DTWM's Pensions Review failings occurred at a time when there was a very high level of awareness within the financial services industry, including Deloitte & Touche, of the issues surrounding the Pensions Review, heightened by much political and public concern; and

vii. DTWM breached Deloitte & Touche internal guidelines by failing to properly inform Deloitte & Touche of any risk issues which might have affected Deloitte & Touche as a whole until 2 September 2002 despite being aware of such issues from 1999. DTWM should have made Deloitte & Touche aware earlier of the concerns with its business. Had it done so, given that Deloitte & Touche did take decisive steps and implemented remedial action when it was eventually aware of these issues, it is likely that Deloitte & Touche would have taken action to prevent or reduce the failings. Therefore DTWM's failure to refer those concerns caused the issues to continue unresolved for a significant period of time.

3.3 Despite the seriousness of DTWM's failings and what the FSA regards as a wholly unacceptable approach adopted by its senior management to compliance up to and

including 2000, the FSA recognises that the size of DTWM's customer base and the extent of its business was not such as to put a large number of customers at risk of substantial financial loss. The FSA also recognises that DTWM (with substantial assistance from Deloitte & Touche) fully co-operated with the FSA during the investigation and, after new management assumed control of DTWM in August 2002, it quickly identified the failings in DTWM's legacy business and took swift and decisive action effectively to close it. In addition DTWM has:

i. worked closely with the FSA over the past two years with a view to implementing appropriate methodologies for identifying and paying redress to disadvantaged customers; and

ii. spent considerable sums in conducting the PBR and is due to complete it in a manner which is both thorough and accurate and should enable all disadvantaged customers to be fully compensated.

3.4 It appears to the FSA, having regard to its statutory objectives, which include market confidence as well as the protection of customers, that the penalty is an appropriate sanction in all the circumstances. Were it not for the mitigating factors described in paragraph 3.3 and for the co-operation demonstrated by DTWM in enabling the early settlement of the matter, the financial penalty imposed would have been substantially greater.

3.5 DTWM's failings may be summarised in the following particular respects:

i. although DTWM implemented a number of compliance arrangements to ensure that its staff complied with the PIA Rules, these arrangements failed to ensure that its financial advisers ("advisers") complied with the PIA Rules relating to suitability and record keeping. DTWM also failed to ensure that its advisers, and their supervisors in turn, were supervised properly;

ii. in addition, the effectiveness of DTWM's compliance structure was seriously affected by the approach to compliance adopted among members of DTWM's senior management up to and including 2000. This approach contributed to the fact that DTWM's compliance structures did not provide a system to ensure compliance with the PIA Rules in all aspects of its business;

iii. although a revised compliance structure (which identified a number of deficiencies in DTWM's sales processes) was introduced in February 2000, it was not effective in ensuring that all issues were rectified;

iv. DTWM failed to take adequate remedial action to address compliance failings highlighted in the PIA's 1999 Supervision Visit report ("the 1999 Supervision Visit report") in relation to documenting information obtained from its clients. This, in turn, contributed to the continuation of these failings;

v. DTWM maintained a centralised compliance function and did not implement a robust compliance structure between 1997 and 1999, sufficient to its business, in relation to the branch structure through which it operated;

vi. DTWM allowed its assistant Compliance Officer to perform the substantive

elements of the Compliance Officer role between April 2000 and February 2001, without being registered with the PIA as such, and thereby failed to comply with the PIA Rules in respect of individual registration referred to in 3.7 (iv);

vii. DTWM put forward as a fit and proper person to become a registered individual with the PIA, a person who had previously expressed an intention to a senior manager with compliance responsibility (who did not inform the Board) to carry out a course of conduct which (had it been proceeded with) might have misled the PIA. By failing to take all necessary steps to satisfy itself of his fitness and propriety DTWM failed to comply with the PIA Rule in relation to individual registration referred to in 3.7 (v); and

viii. while DTWM operated a Training & Competence ("T&C") programme, it was not implemented adequately to ensure that all of its advisers complied with the PIA rules relating to the documentary requirements of giving investment advice and keeping relevant records.

3.6 The failures in DTWM's compliance arrangements are illustrated by the fact that 96.8% of client files reviewed in DTWM's PBR, discussed at paragraph 6.4, did not comply with regulatory requirements relating to the documentation of information from clients and the documentation of advice. In addition, the current results of the PBR indicate that 10% of all Zero Dividend Preference Shares ("ZDPS") cases and 7% of all cases sold by one of DTWM's advisers ("the relevant adviser") were unsuitable. In addition, DTWM's failure to maintain adequate records of investment advice severely hindered its ability to conduct the PBR in a timely manner.

3.7 As a result of the actions described above, the FSA considers that, between 1997 and 2001:

i. DTWM acted in breach of PIA Rule 7.2.1(1)(a) (Monitoring by Members), in its failure to monitor (or monitor effectively) advisers and their supervisors;

ii. DTWM acted in breach of the PIA's requirement to act with due skill, care and diligence in the implementation of a robust compliance structure and accordingly also in breach of SIB Principle 2. This was compounded by the approach to compliance adopted up to and including 2000 among members of DTWM's senior management;

iii. DTWM also acted in breach of SIB Principle 9 in its failure to organise and control its internal affairs responsibly in the implementation of a compliance structure that ensured compliance with Regulatory Rules and that was appropriate to the branch structure which it operated and in its failure to implement fully the remedial action required by the PIA in 1999;

iv. while allowing the assistant Compliance Officer to perform the substantive role of Compliance Officer between April 2000 and February 2001 without being registered with the PIA, DTWM acted in breach of PIA Rules 1.8.8(2)(d) and 1.8.8(5);

v. when DTWM applied to the PIA to place a manager on the Register of Individuals it breached PIA Rule 1.8.9(2) as DTWM failed to satisfy itself, on

reasonable grounds, that he was a fit and proper person to be a registered individual;

vii. by failing to maintain records which showed that its investments were recommended only when they were suitable, DTWM acted in breach of PIA Rule 5.1.1(1); and

viii. by its failure to implement its T&C programme in such a manner that it trained its advisers satisfactorily to ensure they complied with the regulatory requirements relating to the obtaining and keeping of records and ensuring that its supervisors adequately supervised its advisers, DTWM acted in breach of PIA Rule 2.6.1.

Pensions Review

3.8 DTWM failed to take all reasonable steps to carry out its Pensions Review in accordance with the standards and specification prescribed by the PIA. Specifically, DTWM failed to take all reasonable steps to identify its starting population in respect of Phase 1, review cases within the timescales prescribed by the PIA and call properly on the expert resources from within Deloitte & Touche at a sufficiently early stage to assist it with its Pensions Review.

3.9 DTWM failed to take all reasonable steps to identify its starting population in respect of Phase 1. In conducting this work, DTWM relied upon its internal records, which were not adequate to provide all the information required. This resulted in a flawed starting population being created and consequently, DTWM failed to complete either its Phase 1 review or its Phase 2 review within the PIA's deadlines, which it missed by 54 months and 12 months respectively.

3.10 This is particularly serious given that DTWM had a relatively small number of reviewable cases. As at the Phase 1 deadline of 31 December 1998, DTWM had only completed 25% of its Phase 1 cases. DTWM failed to make offers of redress to five policyholders by the Phase 1 deadline. As at the Phase 2 deadline of 30 June 2002, four cases missed the deadline. As at 30 September 2002, DTWM's Pensions Review was still only 79% complete, since additional reviewable cases had been identified.

3.11 Having regard to the size of its Pensions Review and the expert resource it could have called upon for assistance from Deloitte & Touche, the FSA considers that DTWM, by its conduct as set out above, failed to take all reasonable steps to carry out its Pensions Review in accordance with the standards and specifications prescribed by the PIA. DTWM therefore breached PIA Rule 7.2.2.

3.12 DTWM also failed to act with due skill, care and diligence in its conduct of the Pensions Review, in breach of SIB Principle 2.

Training and Competence Arrangements

3.13 DTWM failed to implement a T&C programme appropriate to its business in the supervision of its advisers and supervisors in relation to T&C requirements. In consequence, DTWM breached PIA Rule 2.6.1.

4 BACKGROUND

4.1 DTWM is a private limited company and its entire share capital is owned by Deloitte & Touche, a professional services firm.

4.2 DTWM (then called Touche Ross Financial Services), was regulated by the PIA from 30 December 1994 up to 30 November 2001, and since then has been regulated by the FSA. On 1 August 2002, the firm changed its name (from Deloitte & Touche Private Clients Limited) to DTWM.

4.3 DTWM's registered offices are at Hill House, 1 Little New Street, London, EC4A 3TR.

4.4 On 1 August 2002, a transaction was concluded between Deloitte & Touche and the UK Partnership of Arthur Andersen, as a result of which Deloitte & Touche acquired some of the assets of Arthur Andersen and many of the employees and partners of Arthur Andersen joined Deloitte & Touche. Thereafter, new management took control of DTWM comprising ex-Andersen partners and all but one of the advisers were replaced.

4.5 In August 2002 new management took control of DTWM. Its Board of Directors is now entirely different from the Board as constituted prior to August 2002.

5 DTWM's Business

5.1 DTWM's principal activity during the relevant period was private client tax and trust advisory services to individuals. Throughout the years 1997 to 2001, the turnover of DTWM's regulated investment business was estimated at approximately 10% of DTWM's total revenue. The number of clients of DTWM ranged from 1177 in 1999, decreasing to 640 in 2001.

5.2 During the relevant period DTWM operated 12 branches in the UK, which provided investment advice for some or all of that period. The numbers of staff authorised to give financial advice varied between branches. Many advisers did not however provide regulated advice on a day-to-day basis. The branches in London (33 advisers) and Cambridge (14 advisers) were the largest. DTWM had a total number of between 40 and 60 advisers, of which fewer than 10 advisers on average provided advice in excess of two cases per week.

5.3 As noted above, in August 2002 new management took over the business.

6 DISCOVERY OF CURRENT ISSUES

PBR and Compliance Arrangements

Background

6.1 During a discovery visit on 21 December 2001, the FSA's Supervision Division ("Supervision") was informed by DTWM's Compliance Officer that he considered that DTWM's anti-money laundering arrangements and Know Your Customer ("KYC") record management systems were inadequate, and that DTWM's advisers

had not been adequately advising customers of the risks associated with investments in ZDPS. Consequently, these issues raised concerns over the effectiveness of DTWM's compliance arrangements.

6.2 On 15 January 2002 Supervision informed DTWM of its concerns in relation to DTWM's anti-money laundering arrangements, KYC record management systems and T&C arrangements. Supervision requested DTWM to draw up a project plan to remedy these issues. In respect of the suitability of investment recommendations, it was agreed that DTWM would undertake the PBR to determine whether DTWM had breached any PIA and/or FSA Rules and, if it had, whether loss had been suffered by the clients concerned.

6.3 On 30 January 2002, DTWM provided a plan to the FSA which split the project (known as the "FSA Review") into four review workstreams: anti-money laundering arrangements; examining KYC records; reviewing T&C arrangements; and a PBR in respect of the suitability of investment recommendations.

6.4 The four areas which formed the basis of the PBR were:

i. ZDPS transactions;

ii. Income Drawdown Pensions transactions and Self-Invested Personal Pension Plan transfers ("Pensions");

iii. Switches from a core portfolio holding to another product ("Switches"); and

iv. Advice and sales undertaken by the relevant investment adviser who was an adviser and supervisor in DTWM's Cambridge branch.

6.5 On 17 April 2002, DTWM received a private warning letter from the FSA. Although no formal determination had been made on the issues raised in the FSA's letter of 15 January 2002, the FSA considered that DTWM maintained inadequate controls including record keeping and training; KYC records; and T&C arrangements. In reaching the decision not to discipline DTWM, the FSA took into account remedial work conducted by DTWM at the time.

6.6 Following a meeting between the FSA and DTWM on 9 August 2002, the matter was referred again to Enforcement on 21 August 2002 on the basis that, among other matters, DTWM had failed to identify whether DTWM had breached any PIA and/or FSA Rules and, if it had, whether loss had been suffered by the clients concerned.

Pensions Review

6.7 The PIA was informed that DTWM had missed the deadline for completion of Phase 1 of its Pensions Review in a letter dated 21 October 1999. DTWM informed the PIA that it had identified two additional Phase 1 cases. These cases had been identified as a result of DTWM's population verification exercise in 1999.

6.8 As at the Phase 1 deadline of 31 December 1998, DTWM had only completed eight Phase 1 cases out of its total population of 32 cases, a proportion of 25%. DTWM had also failed to make offers of redress to five Phase 1 policyholders by the Phase 1 deadline.

6.9 On 12 July 2002, DTWM informed the FSA that it had missed the deadline for completion of Phase 2 of its Pensions Review. DTWM stated that Phase 2 was 86% complete (17 Phase 2 cases still required a review), although this figure decreased to 79% in the Return to the FSA for the period up to 30 September 2002. DTWM had also failed to make offers of redress to four Phase 2 policyholders by the Phase 2 deadline.

7 FACTS AND MATTERS RELIED UPON

A. Compliance Arrangements up to and including 2001

Reviews for Suitability and Record keeping

7.1 As a member of the PIA, DTWM was required to implement compliance arrangements to ensure that its advisers complied with the PIA Rules relating to suitability and record keeping. In this regard, DTWM had in place the following measures:

i. *Investment Committee, Products Committee and Pensions Committee (together "the Committees")*

The role of the Committees was to determine which specific product of a particular class was the best performing. The Committees' decisions were communicated to DTWM's investment staff. Advisers with clients who required particular types of investments were obliged to recommend products approved by the relevant Committee, or were limited in choice to the products approved by that Committee.

ii. *Supervisors*

DTWM's supervisors were required to review advisers' correspondence and review at least one client file per year.

iii. *"White" system*

This system required all DTWM correspondence sent to clients to be circulated to all of DTWM's advisers and senior management. Because it was only the advisers' correspondence that was circulated, the other advisers were not in a position to assess whether the advice contained within the letter was in keeping with the underlying information about the client contained within the client file.

iv. *Audit reports from external auditors*

DTWM's external auditors were responsible for ensuring that accounts prepared by DTWM gave a true and fair view of the state of DTWM's affairs. The external auditors had a duty to report to the PIA any circumstances likely to have material significance for determining either whether a person was fit and proper to carry on investment business or whether disciplinary action should be taken in order to protect investors from significant risk of loss. While the external auditors reported to DTWM that client files were well

maintained, it was not the role of the auditors to examine client files to assess whether they complied with the PIA Rules relating to suitability and record keeping.

v. *Reviews by DTWM's Compliance Officer*

Between 1997 and November 1999 DTWM's Compliance Officer had responsibility for ensuring that DTWM's advisers complied with the PIA's requirements. In this regard, he conducted visits to DTWM's branches to conduct audits in accordance with the Compliance Plan, which stated that all of DTWM's branches would be visited annually to ensure compliance with PIA Rules. Between November 1999 and February 2000 DTWM redesigned its audit processes in order to increase the effectiveness of the Compliance Officer's file reviews.

7.2 Prior to February 2000 client files were reviewed during the audits conducted by the Compliance Officer but they were not examined to assess whether specific recommendations made by DTWM's advisers were suitable in accordance with the PIA Rules.

7.3 Files were reviewed for compliance with the PIA's record keeping requirements. Information required from clients to meet these requirements depends on the type of recommendation made and, because the suitability of the specific recommendation was not reviewed by the Compliance Officer, it was not possible for him to determine whether sufficient information had been gathered to enable the adviser to ensure that the particular recommendation was suitable. Reviews of client files in relation to record keeping were therefore ineffective.

7.4 The compliance visit reports indicated that the Compliance Officer had assessed client files for suitability, however, this assessment was limited to assessing whether the recommendation made was one that had approval from one of the Committees, and whether certain key documents were present in the client file.

7.5 Between 1997 and April 1999, the Compliance Officer was the sole resource operating DTWM's compliance function. In addition to his role as DTWM's Compliance Officer, he also acted as DTWM's finance officer. The compliance function was under-resourced during this time and the Compliance Officer had responsibilities other than compliance matters which took up his time. Although *ad hoc* assistance was secured in dealing with certain aspects of his compliance function between 1997 and 1999, this did not extend to the Compliance Officer's primary task of ensuring that advisers acted within the PIA Rules (especially in respect of assessing suitability of recommendations and record keeping).

Conclusion

7.6 While DTWM had in place a number of processes that sought to ensure that staff complied with the PIA Rules relating to suitability and record keeping, the systems implemented did not ensure that client files were reviewed to determine whether the documentation on the files supported the recommendation made and whether they were suitable and, as a result, the review of record keeping was ineffective. The results of these failings are, in part, more fully discussed from paragraph 7.40.

Role of Supervisors

7.7 DTWM did not review the work performed by supervisors within its branches. DTWM's T&C Manual did not contain processes for the monitoring of supervisors' financial advisory roles. In particular, it did not specify how supervisors' financial advice was to be monitored and it did not make provision for the requirement for supervisors to maintain competence if they were to continue providing financial advice.

7.8 DTWM also did not effectively control the number of advisers particular supervisors were responsible for, having regard to the other responsibilities that they had (primarily advising their own clients). In some cases supervisors had to supervise a substantial number of advisers dispersed across several different branches. For example, one supervisor supervised 13 advisers spread across five branches and another supervised 20 advisers, although the majority of these advisers did not provide advice on a day-to-day basis.

7.9 In particular, the relevant investment adviser (who was the main supervisor in the Cambridge branch) had a substantial number (approximately 300) of "high net worth" clients. However, despite the amount of work required to manage their affairs, he also supervised eight advisers in 1999 and 10 advisers in 2001, although the majority of these advisers did not provide advice on a day-to-day basis. As is stated in Section 7B, all of his client files and the advice he gave has been reviewed as part of the PBR, and its findings currently indicate that he mis-sold 7% of his cases. In addition, 75% of his client files contained insufficient KYC information and in 72% of the cases reviewed he had provided the client with a non-compliant Reason Why Letter ("RWL").

Conclusion

7.10 DTWM failed to maintain a compliance system that ensured the effective supervision of its advisers. Its compliance system also did not provide for the monitoring of the work performed by its supervisors.

Approach to Compliance

7.11 The approach to compliance adopted by DTWM's senior compliance management up to and during 2000, did not contribute to a compliance structure or culture that was sufficiently robust or effective in ensuring compliance with the regulatory requirements. In particular, DTWM's senior compliance management believed that the type of business that DTWM operated meant that compliance with many PIA Rules relating to the requirements in relation to the documentation of information from clients and the documentation of advice was unnecessary to ensure that suitable advice was given to their clients. Further, they believed that there was little purpose to be served by checking that advisers had complied with these regulatory requirements.

7.12 DTWM's senior compliance management had reached the conclusions referred to above based upon a number of assumptions about DTWM's business model and DTWM's client base. DTWM's senior compliance management adopted the approach

that DTWM's client base was one that consisted of sophisticated consumers who had an understanding of the investment market, which they believed meant that clients themselves were in a position to assess the suitability of investment advice and that therefore there was less risk of mis-selling. Additionally, DTWM's senior compliance management believed that DTWM could place firm reliance on various factors including the quality of DTWM's advisers and the fact that it did not charge its clients on a commission basis.

7.13 Consequently, prior to the end of 2000, DTWM's senior compliance management believed that there was little need for DTWM to check the quality of advice provided by its advisers. Further, at this time DTWM's senior compliance management held the view that the PIA Rules relating to the documentation of information from clients and the documentation of advice did not contribute to the provision of good investment advice and did not increase the level of protection offered to consumers.

7.14 Further, DTWM's Compliance Officer at the time considered that DTWM's clients simply required assistance with the administrative burden attached to investment business and therefore that the risk of mis-selling to DTWM's clients was diminished.

7.15 The approach to compliance held by DTWM's senior compliance management meant that advisers generally did not regard compliance, in particular compliance with the rules relating to the documentation of information from clients and the documentation of advice, as good business practice and, while some advisers were receptive to the introduction of a revised compliance structure during February 2000, there was unwillingness on the part of some advisers to accept change.

7.16 This attitude to compliance was evident, even when DTWM's Board produced a note in September 2000 in support of the new compliance function and reminding DTWM's advisers of the importance of compliance. One former senior compliance manager and member of the Board attached a covering note (which the full Board were not aware of) to all of DTWM's advisers which, while urging compliance with the Board's message, made it clear that he believed compliance to be a nuisance and that it did not add to the protection of DTWM's clients.

7.17 By October 2000, DTWM's senior compliance management had realised that the approach that they had taken to compliance up until then could not continue. A memorandum sent by one member of DTWM's senior compliance management to his successor advocated the need to increase the amount of compliance resource and, in addition, included a number of admissions concerning his own and DTWM's attitude towards the regulatory requirements to which DTWM was subject to. He admitted, first, that there was a culture of non-compliance within DTWM, secondly, that there was little belief in DTWM (in which he included himself) in compliance; and finally that DTWM had been fortunate to escape adverse consequences given the manner in which the compliance function had been operated in the past.

Conclusion

7.18 The effectiveness of DTWM's compliance function was undermined by the approach to compliance adopted by DTWM's senior compliance management up to and during 2000. Additional compliance resource was introduced in 2000 and a revised system of compliance visits was introduced, which identified a number of deficiencies in

DTWM's selling practices, as discussed below.

The Revised Compliance Structure

Compliance Weaknesses

7.19 A revised compliance structure began to be introduced in February 2000, following the receipt of the 1999 Supervision Visit report. During 2000, as part of this revised structure, compliance audits were conducted at all of DTWM's branches. The audits identified compliance failings throughout DTWM's branches. The internal compliance audit reports in respect of the two largest branches, Cambridge and London, exhibited failure rates of some 72% and 50% respectively in relation to KYC information and some 74% and 48% in relation to RWL failures.

7.20 In addition to highlighting the areas of failure, the audit reports identified the required remedial action which had to be taken by the relevant adviser in order to make the client file compliant. The reports specified that remedial action had to be completed within one month. The deadline for remedial action was rarely met, especially at the Cambridge branch. In addition, in some cases, the required remedial action was insufficient in ensuring compliance (as was highlighted during the PBR).

7.21 The visits also identified weaknesses of a generic and systemic nature in DTWM branches nationwide and that DTWM lacked uniform compliance systems and practices.

Resource

7.22 While the 1999 PIA Supervision Visit report also prompted DTWM to increase available compliance resource, not all of the increased resource was devoted to DTWM compliance work. In particular, and as set out below, DTWM's Compliance Officer acted as such until January 2001, but he had in effect relinquished most of the responsibilities of his role, and was concentrating on his role as DTWM's accountant. Three additional members of staff were recruited to assist a new Compliance Officer, who concentrated on performing the compliance audits described above. This additional resource was not available to the compliance team on a full time basis, as the three recruits spent significant periods of time working on projects outside of the DTWM compliance team. However, by early 2001 DTWM's Compliance Officer did have three full time assistants.

Conclusion

7.23 While the DTWM audits were successful in identifying failings by advisers, they were not effective in ensuring that all issues were rectified. The required remedial action was either not completed or was insufficient to make all cases compliant.

Failure to take adequate corrective action following the PIA Visits

7.24 While the receipt of the 1999 Supervision Visit report led to an enhanced compliance structure, which was more effective in identifying issues with the advice provided by DTWM's advisers (for example suitability, record keeping and accurate RWLs), this did not ensure that these issues did not reoccur.

7.25 The 1999 Supervision Visit report highlighted concerns with the evidence held on client files. In particular, this related to insufficient evidence to demonstrate that the adviser obtained and recorded adequate details regarding the client and that consequently DTWM was unable to demonstrate that it had adequate grounds for believing that the recommendation made was suitable.

7.26 The PBR examined, among other things, cases where recommendations were made after receipt of the 1999 Supervision Visit report. I t has indicated that the failure to obtain and record sufficient KYC information continued to the extent that, to date, in 82% of cases, DTWM has been unable to determine whether the recommendation made was suitable or not. DTWM is therefore obliged to revert to the individual clients to obtain further information before being able to conclude whether the recommendation made was suitable or not.

Conclusion

7.27 DTWM failed to take adequate remedial action to address the compliance failings highlighted in the 1999 Supervision Visit report in relation to information obtained from its clients. This, in turn, contributed to the continuation of these failures.

Branch structure

7.28 DTWM operated through a series of branches and its compliance function was centralised at its Cambridge branch, where its Compliance Officer, up until February 2001, was based. Such a structure required a robust compliance system.

7.29 Between 1997 and 1999 DTWM's Compliance Officer conducted monitoring visits to the Cambridge and London branches more than once a year. However, the client files of the highest producing investment adviser in Cambridge were reviewed as part of the PBR and the evidence to date shows that 7% of his cases may have been mis-sold. When a new Compliance Officer was appointed, he reviewed a number of files in the London branch and found basic compliance shortfalls including inadequate KYC information, deficient RWL's and poor file composition. In particular, he considered that 58% of files reviewed had inadequate KYC information. The Compliance Officer visited other branches annually.

7.30 DTWM did not maintain a system of support for the centralised compliance function in all of its branches. Some of the branches had insufficient resource and/or expertise to support and monitor advisers on a day to day basis.

Conclusion

7.31 DTWM maintained a disparate branch network and a centralised compliance function. Therefore, DTWM's centralised compliance function had to be robust in order to ensure that it could adequately monitor the performance of its advisers throughout its network and to ensure that they complied with the PIA Rules. DTWM did not have such a compliance function between 1997 and February 2000. After February 2000 the compliance function was only able to identify compliance failings after the point of sale and the remedial action prescribed was largely either not completed or was insufficient to ensure compliance.

Failure to disclose information which may have rendered a manager not fit and proper

7.32 In April 2000 a DTWM manager ("the manager") expressed his intention to a senior manager within DTWM with compliance responsibilities ("the senior manager") to carry out a course of conduct which might have resulted in PIA staff being misled. At the time the senior manager was aware that the manager was due to become a senior manager with Compliance responsibility and therefore had to be a fit and proper person to perform this role.

7.33 While the senior manager did not believe the manager's stated intention was serious and while he told the manager he should not carry it out, he did not inform the DTWM Board or take any other action against the manager. Further, he failed to tell the DTWM Board or take other action even when he discovered that the manager by holding more detailed discussions with another manager had progressed his intention. In the event, it was not proceeded with, although this was not as a result of action taken by the senior manager. However, after these events took place the senior manager checked to see that PIA staff had not been misled.

7.34 When the DTWM Board determined that the manager should become a registered individual the senior manager made it clear to the DTWM Board that he did not believe that the manager should be placed on the PIA's Register of Individuals. However, while he informed the DTWM Board of other concerns that he had regarding the manager, he failed to inform the DTWM Board of the manager's intended course of conduct. Therefore, the DTWM Board were prevented from making a proper assessment as to whether the manager was fit and proper.

7.35 Although the DTWM Board was not informed by the senior manager of the manager's behaviour, it remained incumbent upon the DTWM Board to carry out the checks that would have enabled it to discover facts, known to the senior manager, which would have been material to its judgement as to whether to support the manager's application to the PIA for individual registration. These checks were not properly carried out. This failing is aggravated by the fact that the senior manager had made it clear to senior members of the DTWM Board that he did not support the manager's application. Despite this, the DTWM Board did not seek the reasons behind this view. As a result, the DTWM Director who supported the manager's application to be registered on the PIA's Register of Individuals did not disclose relevant information to the PIA.

Conclusion

7.36 When DTWM submitted the manager's application to the PIA, PIA Rule 1.8.9(2) required DTWM to be satisfied, on reasonable grounds, that he was a fit and proper person to be a registered individual. From April 2000, the senior manager had knowledge that demonstrated that the manager may not have been fit and proper. By failing to inform the DTWM Board of this and by the DTWM Board failing to perform sufficient checks on the fitness and propriety of the manager, DTWM failed to comply with the relevant PIA Rule when it submitted its application for that individual to be registered.

Individual registration

7.37 A member of DTWM's staff began assisting DTWM's Compliance Officer in preparation for the PIA Supervision Visit in 2000. The Compliance Officer subsequently agreed, in discussion with the Compliance Director, to relinquish the substantial majority of his compliance responsibilities to this member of staff ("the assistant Compliance Officer") during April 2000 and became the Compliance Officer "*in name only*".

7.38 The Compliance Officer continued to play a minor role, but the assistant Compliance Officer took responsibility for many of the substantive elements of the Compliance Officer's role, in particular the monitoring of advisers. The assistant Compliance Officer conducted this role between April 2000 and February 2001 without being entered on the PIA's Register of Individuals as DTWM's Compliance Officer.

Conclusion

7.39 By allowing the assistant Compliance Officer to perform the role of Compliance Officer between April 2000 and February 2001, without being registered with the PIA, DTWM acted in breach of the PIA Rules.

B. Findings of the PBR as at December 2003

7.40 As at 19 December 2003, out of the 2,946 transactions reviewed as part of the PBR, some 97% were non-compliant primarily because DTWM could not tell after reviewing the transaction whether the recommendation given had been suitable. In relation to the sales of ZDPS, 10% of cases so far reviewed have been mis-sold in terms of documenting the provision of investment advice. Furthermore, the review of the relevant investment adviser's recommendations has currently found that 7% of his cases have been mis-sold.

7.41 Such a large percentage of non-compliant cases illustrates the fact that DTWM failed to take reasonable care to conduct its business with due skill care and diligence and organise and control its affairs responsibly and effectively between 1997 and 2001.

Issues arising in the PBR

7.42 A significant issue arose in the initial stages of the PBR in respect of the identification of an accurate starting population for all customer transactions in each workstream.

7.43 DTWM commenced a population identification exercise in February 2002 by reference to its electronic information system. However, as a result of DTWM's record-keeping failure this database did not hold all relevant customer information. Thus, large scale problems were encountered in identifying all transactions within each workstream as reference had to be made to a variety of manual records held across DTWM's branch network (which were themselves deficient).

7.44 As at December 2003, DTWM is continuing to verify its population and is continuing to review its customer files. It is likely that the initial review of all cases in the PBR will not be complete until mid-2004, with the whole project to be completed some time thereafter.

Conclusion

7.45 The problems encountered by DTWM in establishing an accurate population are a reflection of DTWM's failure to maintain adequate records of the investment advice it provided. The issues surrounding the identification of all relevant records meant DTWM was hindered from conducting a timely PBR which in turn delayed its ability to progress reviewable cases through to redress. The PBR has also revealed mis-selling of ZDPS and sales made by the relevant investment adviser. As at 15 December 2003, DTWM has not made any redress payments to consumers who have suffered loss.

C. Pensions Review

Background

7.46 In October 1994, the Securities and Investments Board ("SIB") set out requirements for all regulated firms to conduct a review of all personal pensions advised on or arranged between 29 April 1988 and 30 June 1994 (known as the Pensions Review).

7.47 The Pensions Review was set up following widespread concerns over the selling practices of personal pensions. PIA Member firms were required to review their advice to determine whether consumers had been mis-sold personal pensions and to offer redress where appropriate.

7.48 The PIA issued its own "Guidance for Review of Past Business" in April and July 1995. This set out the PIA's requirements that all PIA regulated firms had to identify all personal pension plans, Section 32 contracts[1] and Section 226 contracts[2] advised on or arranged during the relevant period, and, where necessary, to perform assessments of compliance, causation and loss. PIA Rule 7.2.2 enabled the PIA to ensure that its members conducted any review of past business in accordance with SIB requirements. The rule gave the PIA power to provide its members with additional requirements on how to conduct the Pensions Review. The SIB and PIA requirements were collectively known as "the Guidance".

7.49 The first phase of the Pensions Review ("Phase 1") concerned cases which were to be reviewed as a priority, where investors were more likely to have suffered a loss as a result of the mis-selling. These would include deceased investors, retired investors (who had begun to draw benefit), or those investors who were close to retirement age.

7.50 The PIA issued Regulatory Update 31 in May 1997, which stated that all Phase 1 cases should be completed (i.e. to the stage where redress was offered and accepted), or closed on legitimate grounds, by 31 December 1998 ("the Phase 1 deadline"). Firms were to ensure that reasonable steps were taken to apply redress as soon as possible.

7.51 The second phase of the Pensions Review ("Phase 2") concerned younger investors

[1] A Section 32 contract was an authorised PIA product used to transfer one Section 226 contract to another.
[2] A Section 226 contract (or a retirement annuity contract, "RAC") was an authorised PIA product which acted as a retirement fund prior to the introduction of personal pensions on 1 July 1988, at which point no new RACs could be opened.

who were further away from retirement than those reviewable under Phase 1 and were therefore less likely yet to have suffered a loss.

7.52 The PIA issued Guidance on Phase 2 in August 1998. In 1999, the PIA stated that all Phase 2 reviewable cases were to have been completed to the stage where investors had been sent an offer of redress, or a letter explaining that redress was not due, by no later than 30 June 2002 ("the Phase 2 deadline").

7.53 If a case, properly assessed, was considered to be either compliant with the Guidance or where no loss had occurred, the firm could legitimately close the case. Further, if the firm could demonstrate that any non-compliance did not cause the loss incurred, the case could also be closed. Certain classes of cases were excluded from the review process.

7.54 The Guidance also stipulated the type of redress that was to be applied in cases where redress was due. The aim of redress was to put consumers into the position they would have been in if they had joined, never left, or never transferred from, their occupational pension scheme.

Starting Population

7.55 The first task that the PIA required its members to complete, in commencing their Pensions Reviews, was the identification of a "starting population". The identification of a firm's starting population was fundamental to the whole Pensions Review. The firm was required to identify every pension sold at the relevant time. All those cases then had to be assessed and a determination made as to whether investors required a review and, if so, whether they had suffered a loss. It was therefore imperative that the process be completed in an accurate and timely way. If all relevant cases were not captured, there was the possibility that investors, who were mis-sold a personal pension and had suffered a loss, would not be compensated.

7.56 The Guidance in 1994 stated that in gathering information firms should first obtain as much of the information required to review cases as possible from its own files and records. A firm then had to take a view as to the reliability of the information for each case under review. If the files and records held adequate and reliable information, then a review could proceed on the information. A firm would approach a product provider or an occupational pension scheme to fill in gaps in records held and to obtain corroboration of information held, where the reliability of the information was in doubt.

7.57 Once a firm had identified its entire starting population, the next stage of the process was to exclude those sales where the investor could not have been disadvantaged, for example, where an investor was self-employed and would have had no occupational pension scheme to join. All cases not excluded from the starting population formed part of the "reviewable population".

7.58 DTWM had a small number of cases to review in comparison with the very large number reviewed by Deloitte & Touche under Pensions Review outsourcing agreements with external clients, dealt with by its fee-earning area called Human Capital Advisory Services ("HCAS").

Phase 1

Starting Population

7.59 In 1995, DTWM commenced its Pensions Review and, instead of constructing a starting population of cases for the purposes of its Pensions Review, it assumed that it could rely on its records to identify all reviewable cases. DTWM therefore went straight to identifying its "reviewable population".

7.60 DTWM believed that it had completed the exercise of identifying its Phase 1 starting population by identifying its reviewable population by the end of the first quarter of 1996. DTWM requested relevant technical staff to review their client lists and to identify those cases which were either transfers or opt-outs or non-joiners, by collating information from 11 of its 17 branches along with commission statements. A record was therefore made of clients who required a review as opposed to clients who were sold pensions. Therefore, between 1995 and 1999, DTWM did not test the accuracy of its whole starting population.

7.61 DTWM's Phase 1 "starting population" has fluctuated and increased significantly during the course of DTWM's conduct of its Pensions Review. The population originally notified to the PIA's Pensions Review Monitoring Department for the period ending December 1995 comprised 21 cases. DTWM stated that this figure had reduced to eight cases by December 1998. In 1999, DTWM reviewed the accuracy of its starting population in anticipation of Phase 2 of the Pensions Review (as further discussed below). As a result of the review exercise, three additional Phase 1 cases were identified, which were not included in the Phase 1 population. In June 2003, the starting population for Phase 1 had increased to 32 cases, an increase of 300% from the number of cases notified to the PIA in 1998.

Phase 1 (Priority Cases) Deadline

7.62 Once the starting population had been identified, the Guidance required firms to identify all priority cases ("Phase 1") within their starting population.

7.63 All Phase 1 cases should have been completed, or closed on legitimate grounds, by 31 December 1998. As this related to priority cases, non-completion of any Phase 1 reviews would have a detrimental effect on pensioners or those who were close to retirement, if they were due redress.

7.64 DTWM confirmed that it had completed Phase 1 of its Pensions Review in a letter to the PIA in 1997. However, in 1999, DTWM reviewed the accuracy of its starting population in anticipation of Phase 2 of the Pensions Review (as set out below) and discovered that it had failed to identify all of its Phase 1 cases and had, consequently, missed the Phase 1 deadline.

7.65 It became apparent that five policyholders, who should have received compensation payments by the Phase 1 deadline, had not done so. DTWM has subsequently made offers of redress to those individuals.

7.66 The DTWM Director with overall control of DTWM's Pensions Review up to October 2000, was unaware that there had been a deadline for the completion of Phase 1 of the

Pensions Review. He was therefore unaware that DTWM had missed that deadline.

Conclusion

7.67 DTWM failed to take all reasonable steps to identify its starting population. DTWM's reliance on its internal records meant that its Phase 1 starting population was not accurate. DTWM did not review its Phase 1 population until 1999, and DTWM did not act with due skill, care and diligence in identifying all its Phase 1 investors.

7.68 DTWM failed to take all reasonable steps to review its cases within the timescales prescribed by the PIA. As at the Phase 1 deadline on 31 December 1998, DTWM had only completed eight Phase 1 cases out of their total population of 32 cases, a proportion of 25%.

7.69 As a result of DTWM's failures, five policyholders did not receive compensation payments by the PIA's deadline. DTWM has subsequently made offers of redress to those individuals.

7.70 Phase 1 of DTWM's Pensions Review was completed by 30 June 2003, 54 months after the Phase 1 deadline.

Phase 2

Phase 2 Population

7.71 Accurate identification of a starting population was essential because if this information was inaccurate any subsequent work by a firm, based on the starting population, would be incorrect.

7.72 DTWM commenced the construction of its Phase 2 population in 1999. The Phase 2 population work included a verification of the Phase 1 population. DTWM believed this was necessary to ensure that all potential priority cases had been included in the original Phase 1 population. It had been recognised that the original starting population might not be robust enough to identify all Phase 2 cases as well as lacking independent verification.

7.73 In March 1999, DTWM had identified 45 Phase 2 cases. In its last Return, submitted to the FSA for the period ending June 2003, DTWM notified the FSA that the starting population for Phase 2 had increased to 230 cases. Following further work, it was found that DTWM had failed to make offers of redress to four Phase 2 policyholders by the Phase 2 deadline.

Phase 2 Deadline

7.74 DTWM failed to take all reasonable steps to carry out Phase 2 of its Pensions Review within the timescale prescribed by the PIA, with the result that DTWM missed the Phase 2 deadline.

7.75 As at the Phase 2 deadline of 30 June 2002, DTWM had identified 125 cases during Phase 2 as requiring a review, but only 108 of these cases (86%) had been completed to an acceptable stage as defined in the Guidance. However, 13 of those cases were

suspended for legitimate reasons. DTWM informed the FSA that on 30 September 2002, DTWM's Phase 2 Pensions Review was only 79% complete and that the number of cases potentially requiring a review had risen to 231 cases.

7.76 Phase 2 of DTWM's Pension Review was completed by 30 June 2003, 12 months after the Phase 2 deadline of 30 June 2002. Four of the Phase 2 cases that missed the PIA deadline were entitled to redress. DTWM has subsequently made offers of redress to those policyholders.

7.77 In late 2001 or early 2002 a further verification exercise identified 1,239 policies that had previously been omitted from the 1995 and 1999 Phase 1 and Phase 2 populations. These policies were then processed by DTWM's exclusions team and subsequently excluded as not requiring a review.

7.78 In early 2002, DTWM considered the Pensions Review population to be complete, but it believed that the underlying documentation and audit trail did not adequately reflect the work undertaken. It therefore conducted a "population validation exercise", which started in May 2002. This validation exercise identified another 1,085 policies which had been previously omitted from the Pensions Review. These policies were considered by the data gathering team and subsequently excluded as not requiring a review.

Conclusion

7.79 Although the 1,239 policies identified in 2001 and the 1,085 policies "identified" in 2002 were subsequently excluded from DTWM's reviewable population, these figures demonstrate the inaccuracy of DTWM's "starting" population. This highlights the failure of DTWM to take all reasonable steps to conduct its Pensions Review in accordance with the PIA's standards.

Resources Allocated to DTWM's Pensions Review

7.80 PIA Guidance required firms to ensure that the task of identifying priority cases was entrusted to a sufficient number of adequately experienced, trained, resourced and supervised staff to enable firms to meet review targets, with work satisfactorily completed as at the deadline dates (31 December 1998 for Phase 1 and 30 June 2002 for Phase 2).

7.81 In June 2000, DTWM's Pensions Review was moved to Glasgow and was conducted by HCAS. However, DTWM retained responsibility for the quality of the work undertaken by HCAS on its Pensions Review.

7.82 Due to the demand for HCAS resources to be allocated to chargeable outsourced client contracts, only one member of staff spent 100% of his time on the DTWM Pensions Review at the beginning of 2001. The remainder of HCAS staff, with the exception of a loss assessor, who was spending 20% of his time on DTWM's Pensions Review, were working on outsourcing work.

7.83 In March 2001, the Compliance Officer sent a memorandum to the Compliance Director which stressed the risks attached to the non-completion of DTWM's Pensions Review. He listed seven main issues, which included the need to identify

and verify the population and to examine all previously excluded cases, as well as the requirement to appoint a senior, experienced project manager to the Pensions Review.

7.84 DTWM suggests that its failure to complete Phase 2 of its Pensions Review arose as a result of DTWM's failure to appreciate sufficiently early on in the Review the particular logistical difficulties that would be required to complete all Pensions Review cases identified in time and the processes that would be required in order to do so. DTWM further claims that this failure included a failure to appreciate, at a sufficiently early stage, that such logistical difficulties and processes might be assisted by the deployment of additional resources, in particular, by seeking additional assistance from the expert resources available within Deloitte & Touche.

7.85 The lack of HCAS resource on DTWM's Pensions Review was highlighted to the Compliance Officer during May 2001. At that stage no resource was allocated to the project and no progress had been made in relation to the Pensions Review since March 2001. During June 2001, the Compliance Officer was informed that the resourcing issue was urgent.

7.86 The resourcing of DTWM's Pensions Review was still an issue by November 2001, when the Compliance Officer (who was then the project manager) was informed that it was unlikely that additional resource would be available soon. However, while DTWM's Pensions Review was experiencing resourcing problems, partners from Deloitte & Touche's Regulatory Consulting Practice were dealing with an external client's outsourcing work, which was conducted by HCAS. During the course of late 2001 and early 2002 significant additional resources were, however, obtained.

7.87 Although the assistant Compliance Officer (who then subsequently became the Compliance Officer) did perform a compliance oversight function during this period, the FSA considers that DTWM's Pensions Review was not managed adequately from November 2000 to July 2001.

Quality Assurance Report, February 2003

7.88 On 21 February 2003, DTWM produced a Quality Assurance Report ("the QA report") on a sample of cases that were reviewed by the DTWM quality assurance team to ensure that they met regulatory requirements.

7.89 The QA report shows that the cases assessed were significantly flawed and it recorded that the work would be open to regulatory criticism. Delays were noted on a number of the sampled cases and the QA report concluded that it was apparent that sufficient resource was not available to progress all of the cases through to settlement within a reasonable timescale.

DTWM's Pensions Review Steering Committee

7.90 DTWM's Pensions Review Steering Committee ("the Pensions Review Committee") met officially for the first time on 18 July 2001 (some 31 months after the Phase 1 deadline and 11 months prior to the Phase 2 deadline). The Pensions Review Committee was set up to ensure that DTWM completed all outstanding Phase 1 cases and met internal DTWM deadlines.

Conclusion

7.91 DTWM failed to take all reasonable steps to review its cases within the timescales prescribed by the PIA. As at 30 September 2002 (3 months after the Phase 2 deadline) DTWM's Phase 2 Pensions Review was only 79% complete out of a total of 231 cases and its Phase 1 Pensions Review was still not complete.

7.92 As a result of DTWM's failings, four policyholders did not receive compensation payments by the PIA's deadline. DTWM has subsequently made offers of redress to those individuals.

7.93 DTWM had a relatively small number of potentially reviewable cases but failed to take all reasonable steps to carry out its Pensions Review in accordance with the standards and specification prescribed by the PIA, in breach of PIA Rule 7.2.2. The result of this was that a total of nine policyholders did not receive offers of redress within the two time limits specified by the PIA for Phase 1 and Phase 2. Specifically, DTWM failed to take all reasonable steps to identify its starting population to review cases within the timescales prescribed by the PIA or to call on expert resources from within Deloitte & Touche at a sufficiently early stage to assist it with its Pensions Review.

7.94 DTWM's reliance on its internal records meant that its Phase 1 starting population was not accurate. DTWM did not review its Phase 1 population until 1999 (after the Phase 1 deadline) and DTWM did not act with due skill, care and diligence in identifying all Phase 1 investors. This led DTWM to miss the PIA Phase 1 deadline. DTWM also missed the deadline for Phase 2 of the Pensions Review.

7.95 The FSA considers that it is unreasonable for DTWM to have missed its deadlines having regard to the size of its Pensions Review and the expert resource it could have called upon for assistance from Deloitte & Touche. DTWM failed to act with due skill, care and diligence in its conduct of the Pensions Review, in breach of SIB Principle 2.

D. T&C Failings

Deficiencies in DTWM's T&C Scheme

7.96 In February 2001 DTWM's Compliance Department acknowledged that the Stage 1 training process for its staff was "*unstructured*". Whilst the T&C Manual stated that the Compliance Officer would provide compliance training to advisers, in practice this consisted solely of him providing oral tests using the same (non-formalised) compliance test prompt-sheet for the assessments of both Stage 1 and Stage 2 advisers.

7.97 There was inadequate evidence of the importance of the role of supervisors in the T&C Manual. In some cases, meetings between participants of the T&C scheme were irregular and advisers only met formally with their supervisors annually.

7.98 DTWM's T&C Manual also did not stipulate that supervisors who provided advice to clients were subject to the same supervisory requirements as advisers (or designated

individuals).

Conclusion

7.99 DTWM failed to implement a T&C programme in such a manner as to ensure appropriate supervision of its advisers and supervisors.

E. Reference to Deloitte & Touche

7.100 It was Deloitte & Touche's policy that DTWM should bring to its attention any risk issues arising from its business which could affect Deloitte & Touche as a whole. Between 1996 and 2001, DTWM's Compliance Officer met with Deloitte & Touche's compliance team on several occasions, in order to update it on issues within DTWM which may have affected Deloitte & Touche.

7.101 However, until August 2002, DTWM failed properly to raise with Deloitte & Touche serious regulatory issues which had arisen in the course of its business. Between 1997 and 1999, PIA reports raised some of the compliance concerns set out above. However, either the reports did not reach Deloitte & Touche or the nature and criticisms within the reports were not properly communicated to Deloitte & Touche which meant that consideration was not given within Deloitte & Touche as to how these issues should be addressed.

7.102 The draft T&C Healthcheck in October 2000 (which reflected the key concerns contained in the PIA reports) contained a number of criticisms of DTWM's T&C arrangements and concluded with a warning that, if the PIA were to conduct a monitoring visit, the implications would be serious. DTWM's Board received the draft T&C Healthcheck report in December 2000 and recommended a significant amount of corrective action based on the report.

7.103 However, despite the fact that the draft T&C Healthcheck report warned that regulatory action could occur because of the failings set out in the report, and despite the fact that any regulatory action would affect Deloitte & Touche, the report was not shown to Deloitte & Touche.

7.104 On 2 September 2002, Deloitte & Touche's Managing Partner, Practice Protection received a memorandum ("the memorandum") from the new CEO of DTWM which referred to serious deficiencies in DTWM's business, many of which are referred to in this Notice. This was the first occasion on which Deloitte & Touche was made properly aware of such deficiencies. On the same day, it was agreed between DTWM and Deloitte & Touche that DTWM's legacy advisers would stop writing new business and the legacy DTWM business closed on 5 September 2002.

7.105 When Deloitte & Touche became aware of the issues as a result of the memorandum, it took swift and decisive action (as referred to above). The FSA considers that, had the PIA and draft internal healthcheck reports been properly raised with Deloitte & Touche it is likely that Deloitte & Touche would have instigated immediate remedial action.

Conclusion

7.106 The FSA considers that DTWM's breaches are aggravated by its failure to bring to

Deloitte & Touche's attention serious regulatory failures on its part until August 2002, thereby precluding any action being taken by Deloitte & Touche to prevent or mitigate the effect of these breaches.

8 RELEVANT GUIDANCE ON SANCTION

8.1 The FSA's policy on the imposition of financial penalties is set out in Chapter 13 of the Enforcement manual ("ENF 13") which forms part of the FSA Handbook. The principal purpose of the imposition of a financial penalty is to promote the high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefit of compliant behaviour.

8.2 Article 8(4) of the Pre-N2 Misconduct Order provides that, where the FSA proposes to impose a financial penalty it must have regard to:

"any statement made by the self-regulating organisation…which was in force when the conduct in question took place with respect to the policy on the taking of disciplinary action and the imposition of, and amount of penalties (whether issued as guidance, contained in the rules of the organisation or otherwise)".

8.3 Relevant PIA guidance is contained in Annex D of "PIA's Approach to Discipline-Statement of Policy" issued in December 1995. In all material respects this required consideration of the same factors as identified in ENF 13. It has been taken into account by the FSA in determining the appropriate sanction in this case.

8.4 The PIA's Statement of Policy, as stated in paragraph 2 of Annex D, makes it clear however that the criteria for determining the level of sanction are not to be applied rigidly:

"Each case is different and needs to be treated on its own merits. It is not possible to apply a mechanistic approach to the determination of the circumstances in which disciplinary action should be taken or of the sanctions to be applied. The criteria…should not be treated as exhaustive. Nor should it be assumed that regard would necessarily be had to a particular criterion in any given circumstances."

8.5 Similarly it is stated in ENF 13.3.4 that the criteria listed in the manual are not exhaustive and all relevant circumstances of the case will be taken into consideration.

8.6 In determining whether a financial penalty is appropriate and its level, the FSA is required to consider all the relevant circumstances of the case. The FSA considers the following factors to be particularly relevant in this case:

8.7 <u>ENF 13.3.3(1): The seriousness of the misconduct or contravention</u>

<u>PIA Guidance: The seriousness of the breaches. The scale of any investor losses and/or the extent to which investors were exposed to risk of such losses</u>

The level of financial penalty must be proportionate to the nature and seriousness of the contravention. The nature of these breaches is described above from paragraph 3

onwards. The FSA considers that the breaches identified in this case were very serious, resulting from systemic weaknesses in DTWM's compliance arrangements and a fundamental lack of adequate management and compliance controls over the conduct of the Pensions Review:

i. DTWM's failings in its compliance arrangements in 2001 and beforehand prevented it from conducting the PBR in a timely manner. This is particularly serious, since the PBR was instigated in response to concerns raised by its Compliance Officer in relation to the suitability of advice that had been given. In such circumstances it is imperative that firms take speedy action first to identify those customers who had been given wrong advice and secondly to ensure that those consumers receive adequate compensation. As a consequence of the record keeping failures, two years after the issues were first identified, DTWM has been unable to pay any compensation to consumers forming part of its PBR;

ii. similarly, the Pensions Review was set up as a result of concerns identified in relation to the selling of personal pensions. DTWM failed to complete its own Pensions Review until long after the industry-wide deadlines. Consequently several consumers suffered delay in receiving compensation;

iii. the breaches occurred over a lengthy period. While they appear to have caused actual disadvantage to a relatively small number of consumers (although in relation to the PBR the lack of progress has meant that few definitive conclusions can be drawn), those due a review of their pension and investment arrangements have been subject to unreasonable and extensive delay. It should be noted that, at the time the remedial work commenced on both reviews, DTWM could not know precisely how many consumers would ultimately be affected; and

iv. DTWM's difficulty in conclusively identifying consumers potentially affected, increases the risk of consumers due redress not being compensated. It also presents risks in respect of DTWM's inability to deal with future complaints by consumers about the quality of the investment advice they were given.

8.8 ENF 13.3.3(2): The extent to which the contravention is deliberate or misconduct was deliberate or reckless

PIA Guidance: Whether the member intentionally or recklessly failed to meet PIA's requirements

The FSA does not assert that DTWM acted deliberately or recklessly in breaching the PIA Rules including Adopted FIMBRA Rules and the SIB Principles. The FSA, nevertheless, considers that DTWM's failings were the result of, and aggravated by, the prevailing attitude prior to October 2000 of DTWM's senior compliance staff towards compliance. It is the responsibility of senior management of regulated firms to ensure that appropriate systems and controls are in place to control their business and ensure compliance with regulatory requirements. In DTWM's case they were content instead to rely on inappropriate assumptions, for example that the sophistication of DTWM's customers was such that their ability to understand the products that were sold to them could be presumed and on the fact that few

complaints were made and that advisers were not paid by commission. DTWM received a number of warnings that its compliance function was ineffective in ensuring that advisers recorded sufficient evidence to justify their recommendations. The warnings contained within the PIA 1999 Supervision Visit report and the 2000 draft T&C Healthcheck, were initially dismissed. Where action came to be taken it was inadequate. The FSA considers that DTWM failed to consider properly and did not fully implement the substantial changes that were necessary to ensure that its compliance function operated effectively.

DTWM's senior managers were made aware of issues concerning the completion of its Pensions Review, particularly lack of resources, and failed to address them adequately. The FSA considers that DTWM's senior management failed properly to appreciate the requirements of its Pensions Review. The FSA considers that it is unreasonable for DTWM to have missed its deadlines, having regard to the size of its Pensions Review and the expert resource it could have called upon for assistance from Deloitte & Touche and the fact that adequate resources were available to work on DTWM's Pension Review but had been deployed to work on the Pensions Reviews of chargeable outsourced client contracts. Additional resources were eventually called upon in late 2001 and during the course of 2002.

8.9 ENF 13.3.3(3): The size, financial resources and other circumstances of the firm.

DTWM is a relatively small firm in terms of number of staff, number of customers and turnover. Therefore, the number of consumers ultimately affected by DTWM's failings is relatively small. However, DTWM's conduct falls short even of what can be properly expected of a similarly sized independent IFA. In particular, DTWM's failure to complete its Pension Review within prescribed deadlines is in contrast to the majority of small IFAs who managed to complete their Pensions Review on time.

Further, DTWM had available to it considerable backing from its parent company, Deloitte & Touche including the expert Regulatory Consulting Practice. It traded with the benefit of the Deloitte & Touche brand and thus raised amongst its clients the expectation that the service it provided to them would be of a high standard. Against that background, the failure by DTWM to make adequate resources available to ensure that adequate compliance procedures, monitoring and training were in place, as well as to ensure that adequate resource was placed on the Pensions Review is particularly significant. DTWM's senior management failed to ensure that Deloitte & Touche's expertise was sufficiently available to DTWM.

8.10 ENF 13.3.3(4): The amount of profit accrued or loss avoided

PIA Guidance: The extent to which, as a result of the breaches, the Member gained a benefit or avoided suffering a loss

Notwithstanding DTWM's failings, the FSA considers that, as and when compensation is paid, there will be nothing to suggest that DTWM will have benefited financially from any investment business mis-sold to customers. However, in nine cases redress was delayed beyond Pensions Review deadlines and DTWM has yet to identify the redress due to customers in the PBR.

8.11 ENF 13.3.3(5): Conduct following the contravention

PIA Guidance: The firm's response once the breaches were identified

As noted above, DTWM's compliance failings were initially identified by the PIA in 1999.

Although initially refusing to accept the validity of the issues identified by the PIA, DTWM took some remedial action. However, the FSA considers that this action was neither timely nor adequate.

During a Supervision visit in December 2001, DTWM's Compliance Officer voluntarily identified several areas of concern with DTWM's systems. DTWM's ability to conduct the PBR has been hindered by the poor quality of its records. DTWM is continuing to review its customer files and has yet to redress any customers who have suffered as a result of mis-selling.

DTWM has co-operated fully with the Enforcement investigation. Were it not for the remedial action taken and for the co-operation demonstrated by DTWM, resulting in the early settlement of the matter, the financial penalty imposed would have been significantly higher.

8.12 ENF 13.3.3(6): Disciplinary record and compliance history

PIA Guidance: The firm's regulatory history

DTWM has not previously been the subject of formal disciplinary action.

As set out in paragraph 6.5, DTWM received a private warning letter from the FSA on 17 April 2002.

8.13 ENF 13.3.3(7)(8): Action taken by other regulatory authorities and the FSA in relation to similar failings

PIA Guidance: The way in which PIA has dealt with similar cases in the past

The FSA has previously fined firms in respect of a combination of some of the breaches committed by DTWM, although it has never previously fined a firm where all above breaches were present concurrently. The FSA has taken into account penalties levied by previous regulators and the FSA in relation to the breaches committed by DTWM.

9 IMPORTANT NOTICES

9.1 This Final Notice is given to DTWM in accordance with Section 390 of the Act.

Manner of Payment

9.2 The Penalty must be paid to the FSA in full.

Time for payment

9.3 The Penalty must be paid to the FSA no later than 9 February 2004, being not less than 14 days beginning with the date on which the Notice is given to DTWM.

If the Penalty is not paid

9.4 If all or any of the Penalty is outstanding on 9 February 2004, the FSA may recover the outstanding amount as a debt owed by DTWM and due to the FSA.

Publicity

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

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

FSA Contact

9.7 For more information concerning this matter generally, you should contact Carlos Conceicao (direct line: 020 7066 1174/fax: 020 7066 1175) or Lize Lombard (direct line: 020 7066 1398/fax: 020 7066 1399) of the Enforcement Division of the FSA.

Julia MR Dunn
Head of Retail Selling
FSA Enforcement Division