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## FINAL NOTICE

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**To: St James's Place Unit Trust Group Ltd**

**Of: St James's Place House,  
Dollar Street,  
Cirencester,  
Gloucestershire, GL7 2AQ**

**Date: 24 November 2003**

**TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("FSA") gives you final notice about a requirement to pay a financial penalty.**

**1. THE PENALTY**

- 1.1 The FSA gave you a decision notice on 24 November 2003 which notified you that, pursuant to section 206 of the Financial Services and Markets Act 2000 ("the Act"), the FSA had decided to impose a financial penalty against you in the amount of £250,000.
- 1.2 St James's Place UK plc ("SJP-UK"), St James's Place International plc ("SJP International") and St James's Place Unit Trust Group Ltd ("SJP-UT") have confirmed that it does not intend to refer the matter to the Financial Services and Markets Tribunal.
- 1.3 Accordingly, for the reasons set out below and having agreed with SJP-UK, SJP International and SJP-UT facts and matters relied on set out below the FSA imposes a financial penalty on you in the amount of £250,000 ("Penalty").

- (1) Rule 7.1.2(1) and Rules 5.1.1(1) and (2) of the Personal Investment Authority (“PIA”) and Principle 9 of PIA’s Statements of Principle (“the PIA Principles”) in the period from January 2000 to 1 December 2001 (“N2”), and
- (2) Rule 3.2.6 in the part of the FSA Handbook entitled *Senior management, systems and controls* (“SYSC”) and Principle 3 of the FSA’s Principles for Businesses (the “FSA Principles”) in the period from N2 to 13 January 2003.

1.4 SJP-UK, SJP International and SJP-UT are referred to collectively in this Notice as “St James’s Place” or “the St James’s Place Companies.”

## **2. RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES**

2.1. Section 206 of FSMA 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) (No2) Order 2001 (“the Pre-N2 Misconduct Order”) provides, at Article 8(2), that the power conferred by Section 206 of FSMA 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 PIA Rules as if the firm had contravened a requirement imposed by FSMA.
- 2.3. PIA Rule 1.3.1(6) provided that a Member of the PIA which failed to comply with PIA Rule 1.3.1(2) or any of the PIA Principles was liable to disciplinary action.
- 2.4. PIA Rule 1.3.1(2) provided that a PIA Member had to obey the PIA Rules. These Rules included certain rules initially promulgated by LAUTRO (a former self-regulating organisation) and described as the Adopted LAUTRO Rules.
- 2.5. The PIA Principles are universal statements of the standards expected of regulated firms that were promulgated by the Securities and Investments Board and applied to PIA Members.
- 2.6. Extracts of the PIA and FSA Rules and Principles relevant to the breaches specified in paragraph 1.3 are attached to this Notice as Appendix A.

## **3. REASONS FOR THE ACTION**

### **Conduct in Issue – Summary**

- 3.1 The FSA decided to impose a financial penalty on St James’s Place in respect of breaches of the PIA and FSA Rules and Principles specified in paragraph 1.3. These breaches related to serious record-keeping inadequacies in connection with recommendations made to customers by their Appointed Representatives to surrender and replace existing investment contracts that had previously been arranged by competitor product providers (these two connected transactions being referred to

together in this Notice as “a replacement sale”) and their monitoring of these transactions.

- 3.2 In particular, deficiencies in the content and implementation of St James’s Place’s procedures for monitoring replacement sales failed to detect, and prevent, serious deficiencies in record-keeping in connection with replacement sales. As a result of these deficiencies it was necessary to obtain further information in order to determine whether the replacement sale was suitable for the investor.
- 3.3 By virtue of the above failings, St James’s Place acted in breach of PIA and FSA Rules and Principles as set out below.
- 3.4 In the period from 1 January 2000 to N2 St James’s Place acted in breach of PIA’s Rules and the PIA Principles in relation to replacement sales as follows:
  - (1) PIA Rule 7.1.2(1) in that it failed to establish procedures with a view to ensuring that its Appointed Representatives carried out their functions in such a way that they complied at all times with the PIA Rules and Principles;
  - (2) PIA Rules 5.1.1(1) and (2) in that it failed to keep records which demonstrated that it had complied with the PIA Rulebook; and
  - (3) Principle 9 in that it failed to organise and control its internal affairs in a responsible manner and to have well-defined compliance procedures.
- 3.5 In the period from N2 to 13 January 2003, St James’s Place acted in breach of the FSA’s Rules and the FSA Principles in relation to replacement sales as follows:
  - (1) SYSC Rule 3.2.6 in that it failed to take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system; and
  - (2) Principle 3 in that it failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
- 3.6 By virtue of these matters, St James’s Place has demonstrated failings that demand a significant financial penalty. These failings are viewed by the FSA as particularly serious in the light of the following factors:
  - (1) the deficiencies were serious in nature. They arose from serious systemic weaknesses in St James’s Place’s processes for monitoring replacement sales. The FSA places very great emphasis on the importance of adequate monitoring systems to ensure compliance with regulatory rules and standards. This requirement is particularly important in relation to replacement sales by virtue of the higher risks they present of inappropriate advice being given;
  - (2) they occurred notwithstanding the fact that regulatory guidance had been issued to the industry during 1994. This guidance reminded firms of the particular importance of implementing appropriate and effective monitoring procedures in replacement sales to ensure compliance with regulatory standards given the high risk they present as outlined above. The FSA is of

the view that it is imperative that, when detailed regulatory guidance is issued, firms and their senior management react to it in a timely and effective manner;

- (3) they were widespread. The size and nature of St James's Place's distribution network meant that the risks associated with these failures affected a large number of consumers;
  - (4) they were not detected by St James's Place. They were only identified by a PIA Supervision visit to SJP-UK during August 2001. This was despite the identification of significant inadequacies in the documentation of replacement sales, and in the monitoring of these transactions, by PIA Supervision ("Supervision") visits to St James's Place during 1996 and 1998. These deficiencies should have alerted St James's Place to the need to ensure that their monitoring processes in respect of replacement business were adequate and operating effectively; and
  - (5) they continued over a prolonged period of time. They occurred from 1 January 2000 and were not fully rectified until 13 January 2003, a year and a half after they were identified by PIA and as a result of the investigation by the FSA's Enforcement Division ("Enforcement").
- 3.7 While the failings in this case merit a significant financial penalty, the FSA considers that they have been mitigated by the co-operation demonstrated by St James's Place and the action taken to address those failings and the cost of doing so.
- 3.8 This action has included since January 2002 appointing an appropriately qualified Skilled Person under Section 166 FSMA (the "Skilled Person") and responding to guidance given by the Skilled Person (referred to more fully in paragraphs 4.22 to 4.25) by bringing about changes to St James Place's existing processes for monitoring replacement business and implementing these processes in a more effective manner.
- 3.9 The Skilled Person concluded that St James's Place:
- (1) recognises that replacement business is a higher risk than most other new business;
  - (2) has appropriately recognised the importance of suitability in giving advice to its clients; but
  - (3) in the past, has not attached enough importance to the maintenance of sound evidential standards of documentation in client specific files.

The Skilled Person did not identify any systemic issues affecting the suitability of replacement business.

- 3.10 Accordingly, St James's Place has received credit for the above in the amount of the financial penalty the FSA proposes to impose. Without this level of co-operation, the financial penalty would, given the aggravating factors described in paragraph 3.6, have been substantially higher.

## **4. BACKGROUND**

### **St James's Place**

- 4.1 The St James's Place Companies operate as a marketing group currently under the name of the St James's Place Group. In the period prior to mid 2002, they traded under the name of the J. Rothschild Assurance Group.
- 4.2 The St James's Place Companies are subsidiaries of St James's Place Wealth Management Group plc ("SJP Plc") which has its registered office at St James's Place House, Dollar Street, Cirencester, Gloucestershire, GL7 2AQ. SJP Plc is a wholly owned subsidiary of St James's Place Capital plc, which is a majority owned subsidiary of HBOS Insurance and Investment Limited.
- 4.3 SJP Plc's principal activity is the provision of a broad range of investment, pension, life assurance and protection products offered by its authorised subsidiaries. The St James's Place Companies are three of these authorised subsidiaries.
- 4.4 The St James's Place Companies were separately registered with PIA until N2 and have since continued to be separately authorised by the FSA. A brief description of each of the St James's Place Companies and its product range is as follows:
- (1) SJP-UK (formerly J. Rothschild Assurance plc) is a public limited company and a UK Life Office. Its core business is the transaction of life and pensions business. SJP-UK was formerly regulated by Lautro from January 1992 to December 1994.
  - (2) SJP International (formerly J. Rothschild International Assurance plc), also a public limited company, is a life assurance company incorporated in Ireland which exercises passport rights to carry on investment activities in the UK as an EEA authorised firm.
  - (3) SJP-UT, a limited company, is a UK collective investment scheme provider. Its core business is the advising and arranging of collective investments.

### ***Product Distribution***

- 4.5 The St James's Place Companies share the same distribution network and market their individual product ranges through a network of Appointed Representatives, known as the St James's Place Partnership.
- 4.6 As at October 2002, the number of their Appointed Representatives totalled 1,330, operating out of 21 office locations across the UK. In addition 119 Sales Managers operated from these office locations.
- 4.7 The Appointed Representatives are commonly recruited from other product providers, sometimes as a result of product providers reducing or closing their direct salesforce. The Appointed Representatives are also recruited from independent financial adviser networks. Newly recruited Appointed Representatives commonly approach their previous clients to recommend investment contracts provided by St James's Place, subject to any relevant contractual restrictions.

- 4.8 The St James's Place Companies are collectively responsible for the conduct of their Appointed Representatives and for monitoring their compliance with regulatory requirements by virtue of PIA and FSA Rules, relevant statutory provisions and their contractual arrangements with their Appointed Representatives.
- 4.9 The St James's Place Companies operate shared compliance arrangements for monitoring the activities of their Appointed Representatives.

## **Regulatory Context**

### ***Regulatory Context of Misconduct***

- 4.10 Since the introduction of the PIA Rules in 1994, firms have been subject to an obligation to establish and maintain appropriate and effective procedures for monitoring the activities of their investment staff and their Appointed Representatives. Regulated firms should be aware of the importance that the FSA places on the existence of effective monitoring procedures.
- 4.11 This obligation has particular importance in relation to high-risk business such as replacement sales, which carry a far higher risk of unsuitable sales and mis-advice than other, non-replacement, business. Due to its increased compliance risk, it is imperative for firms to ensure that their monitoring procedures and controls in respect of replacement sales are adequate and operating effectively.
- 4.12 The importance of the effective monitoring of replacement business was highlighted by guidance issued by LAUTRO on 11 March 1994 (Enforcement Bulletin 30). This emphasises that members who either recruit individual company representatives, or acquire substantial numbers of company representatives from a company that is closed to new business, should take steps to monitor the new business of such individuals given the high risk they present as outlined above. This is especially relevant in the context of continuing company mergers, take-overs, and disposals within the financial services industry.
- 4.13 The Bulletin noted that this area presents high risks to investors and that serious breaches of the Rules could lead to the member being disciplined.
- 4.14 SJP-UK, the FSA's main contact in this case, was the subject of disciplinary proceedings by Lautro on 28 July 1994 on the grounds of deficiencies in its conduct of replacement sales. In response to the Lautro action, SJP-UK set up monitoring procedures that were tailored to replacement sales. Although these issues do not themselves form any part of the grounds for the action taken in this Notice, their existence should have alerted SJP-UK to the need to ensure that its procedures were operating efficiently to avoid a reoccurrence of these past failings and the breaches identified in this case.
- 4.15 During 1996 and 1998, PIA conducted monitoring visits to St James's Place which identified inadequacies in the standard of its documentation in respect of replacement sales and in its monitoring of such transactions. St James's Place revised its processes in these areas as a result of the corrective action that ensued from these visits.

### ***Current Regulatory Context***

- 4.16 The particular risks associated with replacement sales are currently recognised by the inclusion of express requirements to avoid switching customers between products unnecessarily, and to ensure that such transactions are in the customer's best interests, within Rule 7.2.3(4) in the part of the FSA Handbook entitled *Conduct of Business* ("COB"). (It is not, however, alleged that St James's Place has breached this Rule.)
- 4.17 In its Plan and Budget for 2003/4, which does not constitute formal guidance, the FSA emphasised the need for firms, when designing, marketing, and selling products to retail customers, to have a strategy that recognises and mitigates effectively the regulatory risks that can arise, to fulfil their regulatory obligations.
- 4.18 To meet the above aim, and its statutory objective to protect consumers, the FSA has committed to act in any case where weaknesses are found that put consumers' interests at risk.

### **Discovery of Current Issues**

#### ***Focused Visit***

- 4.19 On 29 and 30 August 2001, Supervision staff carried out a focused visit to SJP-UK and St James's Place Financial Services Limited, another of SJP Plc's subsidiaries, accompanied by Enforcement staff at which the current issues were identified.
- 4.20 A report of Supervision's findings ("the Supervision Report") was sent to St James's Place on 30 November 2001. This specified corrective action to address these failings, including the appointment of a suitably qualified third party to conduct:
- (1) a review of a representative sample of replacement business conducted since 1 January 2000, with reporting to the FSA ("the Past Business Review");
  - (2) a reassessment of 32 cases reviewed by Supervision ("the 32 Case Review");
  - (3) a review of its current monitoring activities and the standards applied by the new business monitoring department; and
  - (4) a review of all future replacement sales until satisfied that they were being monitored to a satisfactory standard ("the Future Business Review").

#### ***Enforcement Investigation and Skilled Person Appointment***

- 4.21 The covering letter to the Supervision Report indicated that the issues identified had been referred to Enforcement for investigation.
- 4.22 As part of the Enforcement investigation SJP-UK was required to appoint a skilled person under Section 166 FSMA with appropriate compliance consultancy experience to oversee and report to the FSA on, the corrective action outlined above. The Skilled Person was appointed during January 2002.
- 4.23 The span of the Past Business Review was 1 January 2000 to 31 December 2001.

- 4.24 The Future Business Review was conducted over the period 19 February 2002 to 13 January 2003. These cases had been reviewed by St James's Place's own compliance staff prior to their completion, and had been approved as compliant. St James's Place voluntarily undertook no replacement sales of investment products, save for pensions, over the period December 2001 to 19 February 2002.
- 4.25 The Skilled Person applied the same test to the cases within the Past and Future Business reviews. In particular, it assessed whether the recommendation was suitable and whether the supporting documentation was adequate.
- 4.26 Enforcement staff visited St James's Place's head office in Cirencester during June 2002.
- 4.27 Enforcement conducted a review of the 32 files reviewed by Supervision supplemented by additional information collated by the Skilled Person (the "Enforcement File Review"). In one of these cases the replacement sale recommended did not proceed. Enforcement's findings, as outlined in paragraph 5.1 to 5.18, followed its review of the remaining 31 cases. In two of these cases, the clients surrendered their existing investment but, according to information subsequently provided by St James's Place, this was not as a result of the advice given.
- 4.28 On 7 February 2003, the Skilled Person provided its report to the FSA ("the Skilled Person's Report").
- 4.29 The FSA sent SJP-UK a copy of its draft Investigation Report on 9 May 2003. SJP-UK, on behalf of St James's Place, provided a response to this on 26 June 2003.

## **5. CONTRAVENTIONS OF RELEVANT REQUIREMENTS**

### **(1) Failure to Keep Adequate Records**

- 5.1 In breach of PIA Rules 5.1.1(1) and (2), St James's Place failed to keep its records in such a way as to demonstrate that it had complied with the requirements of the PIA Rulebook. In a large number of cases the inadequate documentation on client files related to factors that are critical to the assessment of a replacement sale's suitability.

### **Facts and Matters Relied Upon**

#### ***The Enforcement File Review***

- 5.2 In all of the 32 cases reviewed by Enforcement, the original customer file contained insufficient information from which to assess fully whether the recommendation was suitable for the customer in that the original documentation did not make sufficiently clear the client's particular circumstances, financial needs and objectives, or how the replacement sale met those needs and objectives. Examples of the inadequacies in the documentation included the following:

- (1) there was conflicting information regarding the customer's attitude to risk. In several cases in which "with-profit" bonds had been replaced by higher risk unit-linked replacement products, it was not clear how the unit-linked funds suited the investors risk profile;



- (2) the reason for switching from with-profits to higher risk unit-linked investments was not clear;
- (3) it was not clear how the replacement contract was more advantageous to the investor than the existing contract, whether in light of cost-effectiveness or otherwise, or whether the investor's objectives could be met by the existing contract. In several cases the recorded reason for the replacement sale was the client's need to mitigate inheritance tax and it was not clear whether this objective could have been met by the existing product; and
- (4) it was not clear whether the client had been made aware of all relevant advantages and disadvantages of the transaction.

***The Skilled Person's Findings***

*The 32 Case Review*

- 5.3 The Skilled Person reported that in each case it was necessary to obtain additional information from the customer or adviser in order to assess fully whether the replacement sale was suitable for the investor.

*Past Business Review*

- 5.4 The Skilled Person conducted a review of past replacement business sales transacted over the period 1 January 2000 to 31 December 2001.
- 5.5 In a significant proportion of these cases the Skilled Person identified that the customer file contained insufficient information from which to fully assess whether the advice was suitable.
- 5.6 The Skilled Person's Report included the following examples of the inadequacies identified from the client records reviewed:
  - (1) the charges on the surrendered and replacement products were not documented as having been disclosed, or a comparison of these charges had not taken place;
  - (2) there was an insufficient explanation of how the recommendation met the investor's recorded objectives;
  - (3) the investor's existing policies were not recorded in sufficient detail; and
  - (4) it was unclear how the investor's attitude to investment risk had been defined.

**(2) Failure to Monitor Appointed Representatives Adequately**

- 5.7 In breach of PIA Rule 7.1.2(1) and SYSC Rule 3.2.6, St James's Place failed to monitor adequately the conduct of its Appointed Representatives in relation to replacement sales. In particular, due to serious deficiencies in the content and implementation of St James's Place's procedures for monitoring replacement sales over the period 1 January 2000 to 13 January 2003, they were insufficient to ensure that its Appointed Representatives complied at all times with regulatory requirements

and failed to prevent the inadequacies in the record keeping described in paragraphs 5.1 to 5.6.

### **Facts and Matters Relied Upon**

#### ***Summary of St James's Place's Monitoring Arrangements in Respect of Replacement Sales***

- 5.8 A Business Monitoring Team, based at St James's Place's head office, monitors and pre-approves potentially higher risk replacement business to ensure its compliance prior to its completion. These cases include the replacement of investment and pension products.
- 5.9 Several Business Quality Managers based at each office location monitor and pre-approve other types of replacement sales considered to be of a lower risk.

#### ***32 Case Review and Past Business Review***

- 5.10 Twenty-eight of the 32 replacement sales (referred to in paragraphs 5.2 and 5.3) and all the cases within the Past Business Review (referred to at paragraphs 5.4 to 5.6) had been pre-approved by St James's Place's monitoring staff and deemed to be suitable for the customers despite the serious inadequacies in the information on the client files identified by Enforcement and the Skilled Person.

#### ***Future Business Review***

- 5.11 During the period 19 February 2002 to 2 September 2002, the Skilled Person reviewed all new replacement sales, prior to their completion, to assess whether the recommendation was suitable and the adequacy of the supporting documentation.
- 5.12 During the first four months of this period, in a very high proportion of cases, the sales were inadequately documented and there was insufficient information from which to fully assess the suitability of the recommendation. In some cases, because the investor's circumstances were inadequately described, the replacement sale appeared to be unsuitable until further information was obtained. These cases had been previously assessed as compliant by St James's Place's own compliance staff, despite these deficiencies.
- 5.13 The Skilled Person identified a number of fundamental deficiencies in the Suitability Letters during the course of the Future Business Review. Again, despite these deficiencies, the Suitability Letters had been approved as compliant by St James's Place's monitoring staff. In particular, the Skilled Person noted that:
- (1) it was "*not evident the investor had been informed of all the factors related to the recommendation*";
  - (2) the letters were "*not always adequate to help an investor understand fully ...the advice they had been given*";
  - (3) the letters were "*not sufficiently always investor-specific*" and "*sometimes consisted of standard paragraphs which were not tailored to the investor's personal circumstance, so that investor-specific reasons were not always*

*given as to why the existing product failed to satisfy their needs or why the recommended replacement product was more suitable”;*

- (4) that *“occasionally, key information was not quantified in sufficient detail, such as:*
  - (a) *“the surrender penalties or Market Value Adjustment (MVA) amount incurred as a result of cancelling the existing plan”;*
  - (b) the level of out-performance required by the SJP funds in order to match the projected fund from the existing scheme;
  - (c) the surrender penalties applicable to *“the first six years ... with an SJP personal pension”;*
  - (d) *“Sometimes information regarding the loss of benefits provided by the existing plan, such as Guaranteed Minimum Pension and the guarantees provided by with profits funds, was often not adequately explained in the letters”.*

5.14 To address these shortcomings, the Skilled Person recommended a review of the *“content and structure of ... Reason Why [Suitability] Letters with the aim of consistently issuing clear, concise, investor-specific letters containing all the relevant advantages and disadvantages of the transaction”.*

5.15 By virtue of the serious deficiencies described in 5.13, the suitability letters and documentation in these cases failed to comply with applicable regulatory requirements and standards. (It is not alleged that St James’s Place actually breached any regulatory requirements, as the deficiencies were rectified before the transactions were completed.)

5.16 As from 2 September 2002, after reporting an improvement in the standard of St James’s Place’s own monitoring processes for replacement business, the Skilled Person reviewed just a sample of new cases.

5.17 On 13 January 2003, after the Skilled Person reported that St James’s Place’s own monitoring processes were operating to an adequate standard, the new business monitoring ceased.

5.18 The Skilled Person’s Report noted that St James’s Place’s monitoring staff in the Business Monitoring Team appeared to have sufficient technical skills for their roles. However, the need for these monitoring staff to assist the Appointed Representatives to bring submission papers up to a compliant standard distracted the staff from their role of assessing the overall compliance of the replacement advice. This reduced the effectiveness of the staff’s monitoring function.

## **6. BREACHES OF PRINCIPLES**

6.1 By virtue of the extent and severity of the failings and Rule breaches identified above and the prolonged period over which they continued, together with St James’s Place’s failure to identify the serious inadequacies in its monitoring procedures in respect of replacement sales and to remedy the problems without the intervention of the FSA

(despite the regulatory measures highlighting the importance of effective monitoring of replacement business and the identification of similar problems during past Supervision visits) St James's Place has failed to meet its regulatory obligations under the PIA and FSA Principles as set out below:

- 6.2 In breach of Principle 9 of the PIA Principles, St James's Place did not organise and control its internal affairs in a responsible manner and did not have well-defined compliance procedures over the period 1 January 2000 until N2.
- 6.3 In breach of Principle 3 of the FSA Principles, St James's Place did not take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems over the period from N2 to 13 January 2003.

## **7. RELEVANT GUIDANCE ON SANCTION**

- 7.1 In determining whether a financial penalty is appropriate and its level, the FSA is required to consider all the relevant circumstances of the case. Paragraph 13.3.3 of the Enforcement Manual and Annex D of "PIA's Approach to Discipline – Statement of Policy" that was issued in December 1995 indicate the factors that may be of particular relevance in determining the level of a financial penalty. These are discussed below by reference to the circumstances of this case.

- 7.2 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)".*

- 7.3 In all material respects, the relevant PIA guidance, contained in Annex D of "PIA's Approach to Discipline – Statement of Policy" issued in December 1995, required consideration of the same factors as are identified in Chapter 13 of the Enforcement Manual. Both have been taken into account by the FSA in determining the appropriate sanction in this case.

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

*"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".*

- 7.5 Similarly, it is stated in Chapter 13 of the Enforcement Manual at paragraph 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.

The FSA considers the following factors to be particularly relevant in this case.

***ENF 13: The seriousness of the misconduct or contravention.***

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

- 7.6 The level of financial penalty must be proportionate to the nature and seriousness of the contravention.
- 7.7 Although the Skilled Person has not identified any systemic issues affecting the suitability of replacement business, this case has identified serious and systemic weaknesses in St James's Place's shared compliance controls relating solely to replacement business and their implementation. It has long been recognised by the industry, and its regulators, that replacement selling carries a far higher risk of unsuitable sales and mis-advice than ordinary non-replacement business. This is demonstrated by the fact that it was the subject of the specific LAUTRO guidance referred to in paragraph 4.12 and remains the specific subject of COB Rule 7.2.3(4). Due to the greater compliance risk it was incumbent on St James's Place to ensure that its procedures and controls in respect of replacement sales were fully implemented and operating effectively.
- 7.8 The deficiencies in the compliance processes continued over a prolonged period of time – from January 2000 until 13 January 2003 - and were not detected by St James's Place. They were identified by a Supervision visit to SJP-UK during August 2001, over a year and a half after they commenced. This was despite the disciplinary proceedings previously taken by LAUTRO against SJP-UK during 1994 on the grounds of similar failings and the identification of significant inadequacies in St James's Place' monitoring processes for replacement business and in the documentation in these transactions, by Supervision visits conducted during 1996 and 1998. These deficiencies should have alerted St James's Place to the need to ensure that its monitoring processes in respect of replacement business were adequate and operating effectively.
- 7.9 The consequence of the monitoring inadequacies was that St James's Place failed to detect, and prevent, persistent and widespread inadequacies in key aspects of the documentation in replacement sales advised by its Appointed Representatives over a prolonged period. These inadequacies in the records related to factors that were fundamental to the assessment of suitability of these transactions for the investors concerned. In some cases, because the investors' circumstances were inadequately described in the original file, the replacement sale appeared to be unsuitable until further information was obtained.
- 7.10 These failings accordingly exposed investors to the risk of surrendering existing investment contracts and committing money to new investment contracts in circumstances where this may not have been in their interests.
- 7.11 The failings were widespread in nature – they affected business written by all three of the St James's Place Companies and were UK wide – and the risks associated with these failures affected an estimated 2,300 clients per annum (the approximate number of replacement business cases transacted annually by St James's Place). However, no evidence was identified of widespread consumer loss as a result of these failings and no further review of past business has been recommended.

***ENF 13: The extent to which the contravention was deliberate or reckless***

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

- 7.12 St James's Place did not deliberately contravene FSA's Rules or PIA's requirements, but the inadequacies in its systems and controls did continue over a considerable period of time, despite the identification of similar deficiencies in the disciplinary proceedings previously taken by LAUTRO against SJP-UK during 1994 and during the Supervision visits conducted to St James's Place during 1996 and 1998.

***ENF 13: The size, financial resources and other circumstances of the firm or individual***

***PIA Guidance: The Member's ability to pay***

- 7.13 The St James's Place Companies are members of one of the UK's largest financial services groups. There is no doubt regarding their ability to pay the proposed penalty.

***ENF 13: Conduct following the contravention***

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

- 7.14 The general policy of the FSA is that firms are given significant reductions in penalty or other proposed disciplinary measures where the seriousness of the non-compliance is mitigated by a proactive response from the firm after the breaches are identified.
- 7.15 The breaches were initially identified by a Supervision visit in August 2001, but were not fully rectified until January 2003. However, St James's Place is considered to have co-operated fully in the Enforcement investigation and in conducting remedial action where required, including the appointment of a Skilled Person and responding to the recommendations of the Skilled Person. In addition by moving quickly to agree the facts of the case and to settle the matter it has helped the FSA to work expeditiously towards its statutory objectives.
- 7.16 Accordingly, these are factors that have been taken into consideration in setting the financial penalty.

***ENF 13: Action taken by other regulatory authorities and the FSA in relation to similar findings***

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

- 7.17 Both the predecessor regulators of St James's Place, LAUTRO and PIA, and the FSA, have taken action against firms for systems and control failings, including compliance and conduct of business failings, which has included the imposition of financial penalties. In determining the level of penalty proposed to be imposed in this case, the FSA has taken these cases into account together with all the particular circumstances described in this Notice.

## **8. IMPORTANT NOTICES**

8.1 The Final Notice is given to you in accordance with section 309 of the Act.

### **Manner of payment**

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

### **Time for payment**

8.3 The Penalty must be paid to the FSA within 14 days beginning with the date on which the notice is given to you.

### **If Penalty not paid**

8.4 If all or any of the Penalty is outstanding after 14 days, the FSA may recover the outstanding amounts as a debt owed by you and due to the FSA.

### **Publicity**

8.5 Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the 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 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 you or prejudicial to the interests of consumers.

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

### **FSA Contacts**

8.7 For more information concerning this matter generally, you should contact Helena Varney at the FSA (direct line: 020 7066 1294/fax: 020 7066 1295).

Julia MR Dunn  
**Head of Retail Selling**  
**FSA Enforcement Division**

## Rules and Principles Breached

PIA Rule 7.1.2(1) provided:

*A Member must establish procedures... with a view to ensuring that its investment staff and other employees and its appointed representatives and their employees carry out their functions in such a way that the Member complies at all times with the Rules and Principles.*

PIA Rules 5.1.1 (1) and (2) provided:

- (1)(a) *A Member must keep records which are sufficient to show at any time that it has complied with the requirements of the Rule Book,...*
- (2) *In particular (but without limiting the generality of (1) above) a Member must keep records of the matters specified in column 1 of Table 5 below and include in them the details specified in column 2 of that Table.*

Principle 9 of the PIA Principles provided:

*A firm should organise and control its internal affairs in a responsible manner, keeping proper records, and where the firm employs staff or is responsible for the conduct of investment business by others, should have adequate arrangements to ensure that they are suitable, adequately trained and properly supervised and that it has well-defined compliance procedures.*

SYSC Rule 3.2.6 (“Compliance”) provides:

*A firm must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system....*

Principle 3 of the FSA Principles provides:

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

## Relevant Regulatory Standards and Requirements

PIA Rule 1.3.9 provided:

- (1) *A Member must accept responsibility, to the same extent as if the Member had expressly authorised it, for anything said, written, done or omitted by any of its investment staff or other employees in the carrying on of the Member’s relevant business;*
- (2) *by any of its appointed representatives or their investment staff or other employees in carrying on the investment business for which the Member has accepted responsibility in writing, or by any person held out by the Member as being its appointed representative.*



Paragraph L6(e) of Schedule L2 of the Adopted Lautro Rules provided:

*A company representative who, in the course of any relevant investment business, has dealings with an investor –...*

- (e) shall not advise the investor to convert, cancel or allow to lapse any investment contract or realise any investment under an investment contract unless the representative has previously –*
  - (i) made a comprehensive study of the investor’s need to make any investment and of his financial resources; and*
  - (ii) disclosed to the investor all relevant consequences and disadvantages likely to follow from the action advised including ...;*

*and the representative shall not in any event advise the taking of such action unless he bona fide believes it to be in the interests of the investor.*

Paragraph L8(1) of Schedule L2 of the Adopted Lautro Rules provided:

*A Company representative shall, in advising an investor as to the suitability for that investor of any investment contract, have regard, in particular, to the investor’s financial position generally, to any rights he may have under an occupational pension scheme or the State earnings-related pension scheme, (if such rights are relevant in the particular case) and to all other relevant circumstances and he shall use his best endeavours to ensure:*

- (a) that he recommends only that contract or those contracts which are suited to that investor; and*
- (b) that there is no other contract available from the Member, or, if the Member belongs to a marketing group, from any member of that group, which would secure the investor’s objectives more advantageously.”*

PIA Table 5, Part III Transactions, paragraph 1(c):

*... sufficient information to show that the transaction was suitable and that the product was as advantageous to the customer as any in the product range; and*

PIA Table 5, Part III Transactions, paragraph 5:

*... a record of the reason for disposal (of any packaged product) and of disclosure to the investor of consequences and disadvantages.*

COB Rule 5.2.5 of the FSA Handbook (“Requirement to know your customer”) provides:

*Before a firm gives a personal recommendation concerning a designated investment to a private customer, or acts as an investment manager for a private customer, it must take reasonable steps to ensure that it is in possession of sufficient personal and financial information about that customer relevant to the services that the firm has agreed to provide.*

COB Rule 5.2.9 (“Record keeping: personal and financial circumstances”) provides:

*A firm must make and retain a record of a private customer’s personal and financial circumstances that it has obtained in satisfying COB 5.2.5R. The record must be retained for a minimum period after the information is obtained, as follows:*

- (1) indefinitely for a record relating to a pension transfer, pension opt-out or free-standing additional voluntary contribution (FSAVC);*
- (2) six years for a record relating to a life policy, pension contract or stakeholder pension scheme;*
- (3) three years in any other case.*

SYSC Rule 3.2.20(1) (“Records”) provides:

*A firm must take reasonable care to make and retain adequate records of matters and dealings... which are the subject of requirements and standards under the regulatory system.*

COB Rule 5.3.5(1) (“Requirement for suitability generally”) provides:

- (1) A firm must take reasonable steps to ensure that it does not in the course of designated investment business:
  - (a) make any personal recommendation to a private customer to buy or sell a designated investment; or*
  - (b) effect a discretionary transaction for a private customer.**

*unless the recommendation or transaction is suitable for the private customer having regard to the facts disclosed by him and other relevant facts about the private customer of which the firm is, or reasonably should be, aware.*

COB Rule 7.2.3(4) (“Restrictions on dealing and switching”) provides:

*A firm must not:*

- (4) make a personal recommendation to a private customer to switch within a packaged product or between packaged products, or make or arrange a switch that gives effect to such a recommendation;*

*unless the firm has taken reasonable steps to ensure that the deal or switch is in the customer’s best interests, both when viewed in isolation and when viewed in the context of earlier transactions.*

COB Rule 5.3.14 (“Contents of a suitability letter”) provides:

*If, following a personal recommendation by the firm, a private customer:*

- (1) buys, sells, surrenders, converts, cancels, or suspends premiums for or contributions to, a life policy or a stakeholder pension scheme; or*
- (2) elects to make income withdrawals; or*
- (3) acquires a holding in, or sells all or part of a holding in, a scheme; or*
- (4) enters into a pension transfer or pension opt-out from an OPS;*

*the firm must provide the customer with a suitability letter, within the time period stipulated by COB 5.3.18R, unless one of the exceptions in COB 5.3.19R applies.*

COB Rule 5.3.16 (“Contents of a suitability letter”) provides:

*The suitability letter in 5.3.14R must:*

- (1) explain why the firm has concluded that the transaction is suitable for the customer, having regard to his personal and financial circumstances;*
- (2) contain a summary of the main consequences and any possible disadvantages of the transaction;*