SQUIRE SANDERS

THE FCA GETS TOUGH ON UNSUITABLE ADVICE AND POOR SYSTEMS AND CONTROLS

Before the Financial Conduct Authority ("**FCA**") took over from the Financial Services Authority ("**FSA**") earlier this year, the regulator had confirmed that the enforcement policy of "*credible deterrence*" (taking tough, targeted effective public enforcement action against misconduct as a way of changing market behaviour) would continue.

The "credible deterrence" policy has underpinned the regulator's approach to enforcement for some five years now and is being taken forward by the FCA precisely because it is considered by the regulator to have been very successful.

Sesame Fine

Further evidence of the regulator's intent came on 5 June 2013 when the FCA announced another large fine, £6,031,200, this time for the well-known financial advisory firm, Sesame Limited.

This was for failing to ensure that the investment advice given to customers was suitable and for failings in systems and controls that governed the oversight of Sesame's appointed representatives ("**ARs**").

Unsuitable Advice

A small part of Sesame's fine, £245,000, related to selling Keydata's products.

Between July 2005 and June 2009, Sesame advised 426 customers to invest a total of over £6,100,000 in Keydata's life settlement products. However the FCA found that the vast majority of Sesame's sales were flawed because (a) there was a mismatch between customers' stated investment objectives, attitude to risk and the products sold; and/or (b) the suitability letters provided to customers stated incorrectly that income or capital growth was guaranteed; and/or (c) customers were incorrectly advised that the Keydata products were low risk.

Weaknesses in Systems and Controls

The substantial element of Sesame's fine was for systems and controls weaknesses.

The FCA found that Sesame had failed to take reasonable care to organise and control its affairs responsibly and effectively and had failed to improve the oversight of its ARs.

In particular, the FCA said that Sesame had failed to identify and monitor sales of those products and funds which were not suitable for most customers; both desk based file reviews and visits by Sesame's internal compliance team were not always suitably robust and there were continuing problems with record keeping for ARs. The FCA added that in terms of Sesame's culture, the language used within the firm *"supported an incorrect view that its customers were the ARs rather than the end retail customers"*. The FCA found that these failings meant that unsuitable sales that occurred between 2005 and 2009 could have been repeated in relation to other investment products between July 2010 and September 2012.

Tracy McDermott, the FCA's Director of Enforcement and Financial Crime, said that Sesame described itself as perfectly placed to deliver expert guidance and services but that the failings in this case fell far short of that. She added:

"The weakness in Sesame's systems and controls showed there was an ongoing risk that unsuitable advice could be given by Sesame's ARs…By allowing ARs to use their regulated permission to operate, Principals are effectively vouching for them. Therefore they must keep a close eye on what ARs do and keep them up to date with the regulator's expectations. Critically, they must also act decisively when things go wrong. Sesame failed on all of these counts."

Sesame agreed to settle the case at an early stage of the investigation and therefore qualified for a 30% discount. Without that discount, the fine would have been £8,616,000.

Ever Higher FCA Fines?

The FCA had previously signalled that cracking down on failings in a firm's systems and controls would be an enforcement priority for the new regulator and the Sesame fine is a further declaration of intent. But it is also worth noting that, with the policy of "*credible deterrence*" continuing to feed through into ever higher fines, the value of combined FSA/FCA fines for the year so far stands at over £150 million.

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