

SUPERVISORY NOTICE – Suspension of immediate effect –
Variation of Part IV permission – Threshold Condition No.4
– Failure of Applicant to maintain PII – Whether
Supervisory Notice varying permission should be suspended
pending hearing of reference – No – FS&MT Rules 2001
No.2476 r.11(1)(e)

HPA SERVICES Applicant

- and -

FINANCIAL SERVICES AUTHORITY Respondents

Tribunal: STEPHEN OLIVER QC

Sitting in public in London on 5 March 2003

Robert Morfee, solicitor, of Clarke Willmott & Clarke, for the
Applicant

Stephen Greenhalgh, for the Respondents

1. This is an application by HPA Services, the Applicant, for a direction suspending the effect of a Supervisory Notice dated 30 January 2003. The Application was heard on 5 March 2003. At the end of the hearing I dismissed the Application giving oral reasons. On 6 March 2003 I issued a written direction dismissing the Application.

2. The Authority then filed their statement of case (on 26 March 2003). The Applicant was required to file a written reply within 28 days of that. As no reply had been lodged by 9 May I notified the Applicant that I had in mind to dismiss the reference unless I receive representations as to why I should not do so. The Applicant has made no representations save to ask for reasons for my decision to dismiss the Application to suspend the immediate effect of the Supervisory Notice.

3. On 3 July 2003 the Applicant wrote to the Tribunal saying that written confirmation of the oral decision had not been received by him. It appears that he is no longer instructing the solicitors who represented him at the hearing of the Application. In this decision I shall summarize the background to the Application heard on 5 March, and will set out more fully the reasons for dismissing it.

4. The Applicant is a sole trader operating as an independent financial adviser. The proprietor of the business is Mr P J Halfpenny who also gave evidence at the hearing of the Application. On 1 December 2001 he was

given permission by the Financial Services Authority (“the Authority”) under Part IV of Financial Services and Markets Act 2000 (“the Act”) to carry on the following regulated activities:

- advising (excluding pension transfers and opt-out) ,
- agreeing to carry on a regulated activity,
- arranging deals and investments and
- making arrangements

Prior to that date the Applicant had been a member of the PIA. In granting the permission referred to above, the Authority was bound by the Act to ensure that the Applicant satisfied and would continue to satisfy the Threshold Conditions set out in Schedule 6 to the Act. Permission given by both authorities was given on the condition that the Applicant maintained professional indemnity insurance (“PII”): see for example Rule 13.1.3 of the Authority’s Interim Prudential Sourcebook for Investment Firms.

5. The Applicant’s PII expired on 30 April 1999. The Applicant has continued to trade since then without PII cover. The Authority issued a Supervisory Notice on 30 January 2003 removing all regulated activities from the permission previously granted under Part IV of the Act. It also issued a warning notice pursuant to section 45(3) of the Act. The Supervisory Notice was stated to take immediate effect in accordance with section 53 and it required the Applicant to notify clients that it was no longer permitted to carry on regulated activities.

6. The Authority’s action is based on their determination that the Applicant no longer satisfies the relevant Threshold Conditions and in particular that the Applicant does not have adequate resources to carrying the regulated activity. As the Applicant no longer meets the test for Part IV for authorization (section 41(2)), the Authority has exercised its power varying the Part IV permission “in order to protect the interest of consumers or potential consumers” (section 45(1)(c)).

7. In this connection I should mention the Authority’s policy in exercising its own-initiative power to vary Part IV permission (ENF3). Section 3.5.2 of ENF3 requires the Authority to have regard to its regulatory objectives and the range of regulatory tools available to it. The Authority’s general approach is, as well as complying with its own regulatory objectives, to have regard to the responsibilities of the management of a particular firm to deal with concern about the firm and to adhere to the principle that a restriction imposed on a firm should be proportionate to the objectives that the Authority is seeking to achieve.

8. The Authority’s approach in urgent cases is to exercise its own-initiative power as a matter of urgency under

section 53 of the Act where, for example, information indicates "significant loss, risk of loss or other adverse effects for consumers, when action is necessary to protect their interests": see section 3.5.12 of ENF3 which states that the Authority should also take into account the impact that a variation of permission may have on a firm's business. The present Application is directed solely at the question of the immediate effect of the Notice served on the Applicant. To determine this I need to review the basis of the Authority's decision to make the direction contained in the notice. In essence this is founded on three conclusions reached by the Authority in relation to the circumstances set out in the next paragraph of this decision (which sets out a chronological summary of events). The first conclusion was that by failing to effect compliant PII cover, the Applicant had failed to make adequate provision in respect of its liabilities, including contingent and future liabilities; the Applicant has therefore failed to satisfy the "adequate resources" condition (Threshold Condition No.4). The second conclusion is that the risk of loss or other adverse effect on consumers by the Applicant's failing causes the Authority to have serious concern about the Applicant's firm such that the immediate suspension is an appropriate response. The third conclusion is that the Part IV permission should take immediate effect to address the Authority's serious concern that claims for which the Applicant is uninsured might arise from new investment business.

Chronological summary of facts as relied upon by Authority

9.1 In 1999 the Authority wrote to the Applicant advising him of the absence of cover and the Applicant wrote back saying that non-renewal had been the result of his father's death, but he was expecting replies from brokers within three days. The Authority wrote informing the Applicant that PII cover had to include pension transfer business.

9.2 The PII Monitoring Unit made further enquiries of the Applicant in late 1999 and early 2000 seeking confirmation of PII cover.

9.3 In April 2000 the Applicant wrote to the Authority stating that he was awaiting confirmation of cover. The Authority by further letters pressed the Applicant for evidence of cover. In July 2000 the Applicant told the Authority that cover had been declined by three insurers because business was too small and because the firm was involved in pension reviews. (He had apparently been required, as part of the review, to write to all his pension clients informing them of their rights to complain and of their opportunities to make claims: this followed from the more general Authority campaign over pension mis-selling.)

9.4 No further action by the Authority appears to have been taken until mid-2002. The PII Monitoring Unit wrote

five letters between June and August 2002 warning the Applicant that PII cover was mandatory and requesting evidence of cover. The Applicant was warned of the possibility of variation or cancellation of its Part IV permission.

9.5 On 20 September 2002 the PII Monitoring Unit wrote (in response to an enquiry from the Applicant) confirming to the Applicant that the Authority would not accept PII with an exclusion for pension review claims. The same day the Applicant had written to the Authority asking for confirmation that such exclusion would be permissible.

9.6 On 26 September 2002, in response to a telephone call from the Authority, the Applicant provided information of all correspondence that it had had with brokers to obtain cover together with application forms. The Authority's letter had explained that if the Applicant had not provided evidence by 31 October 2002, a referral to the Authority's enforcement division would be made.

9.7 On 27 September 2002 the Applicant sent an e-mail to the Authority from a broker stating the broker's belief that the Applicant would not be able to obtain cover without an exclusion for pension review.

9.8 On 31 October 2002 the Applicant wrote to the Authority observing that the Authority had amended its rules in relation to PII cover and asking for a copy of the modified rules so that the Applicant could again explore the market for PII cover. The Authority replied on 5 November giving the Applicant 10 days to see if the new rules made any difference to his ability to obtain cover.

9.9 On 14 November 2002 the Applicant wrote to the Authority stating that it had not been able to obtain cover and requesting confirmation that no punitive action or restriction of trade would be imposed on it. On 18 November the Authority wrote back saying that matters would be referred to "Enforcement" if the Applicant did not provide evidence of cover by 20 November. That letter was followed by a telephone call from the Authority on 19 November stating that further consideration would be given by the Authority.

9.10 A letter of 27 November from the Authority stated that further consideration had been given, but the matter had been referred to Enforcement. The letter addressed an allegation by the Applicant that the Authority had, on an earlier occasion, instructed the Applicant not to progress the pensions review in the absence of PII cover and the Applicant's assertion that that failure to complete the review had been preventing the Applicant from obtaining cover. The relevant part of the Authority's letter reads as follows:

"When we spoke last week, you explained that one of the reasons you are not able to obtain cover is because you have not completed the Pension Review. You said that this was because you were told by the FSA not to progress this work in the absence of compliant PII cover. I can find no record of anyone at the FSA having told you to stop work on your pension review cases. If you have any evidence to support your assertion that you were told to stop, then please send it to me. The position is that you are required to progress the pensions review, despite your lack of PII cover. I urge you to progress the review of the cases identified as quickly as possible, so that consumers affected can know the outcome of the review and receive any redress that may be due to them."

9.11 Then on 6 December 2002 the Applicant was informed by Enforcement that it was preparing to take action. The Applicant wrote back repeating the allegation that the Authority had instructed it not to proceed with the pension review and stating that the information had come from the PIA members' pension review helpdesk. A letter from the Authority of 13 December 2002 set out its belief that the Applicant had not been advised to stop its pension review while it had no PII cover.

9.12 The Applicant wrote on 12 December offering to voluntarily suspend his regulated activities. The Authority by letter of 13 December gave the Applicant until 24 December.

9.13 The Regulatory Decisions Committee of the Authority met on 29 January 2003. It decided that variation action should be taken against the Applicant and that having regard to the Authority's statutory duty to protect, such variation should be with immediate effect.

10. Mr Halfpenny in evidence insisted that he had contacted the helpdesk in 2000 and been told not to progress the pension review until he had cover. It is true, I note, that the Applicant's letter to the PIA of 21 July 2000 states that "We are instructed not to offer any pension compensation settlements until we have PII cover in place". But that is not saying that the Applicant had been told not to progress the pension review. The Applicant's allegation is, I think, both unsubstantiated and too improbable. I do not therefore accept it. More to the point, I cannot see how this allegation, which has been considered in correspondence with the Authority, affects the present issue, namely whether immediate effect of the Notice should be suspended. Mr Halfpenny explained that he had notified his 25 pensions clients of their rights under the Pension Transfer Review project. Nine of these had responded and asked for reviews and these he had declared as potential liabilities. That was why he had not been able to get PII

cover.

11. The Applicant's actual grounds for claiming suspension of the Authority's Supervisory Notice are set out in his Reference Notice as follows:

"I apply for a direction suspending the effect of the Authority notice on the following grounds. In 21 years professional service to this industry I have never had any claim against me by a consumer nor complaint likely to lead to a claim. Suspension of my business activities during my tribunal appeal period is unwarranted. The FSA have allowed me to trade for 3½ years without professional indemnity insurance cover. Circumstances during the appeal are no different to those prevailing since May 1999 and suspension of my ability to generate income is detrimental to preparation of tribunal appeal. There is no appreciable additional risk to consumers by lifting my suspension until a tribunal hearing and decision."

I take into account the Applicant's assertion that he has never had any claim against him nor complaint likely to lead to a claim. But the fact is that the Applicant has been conducting his business without the professional indemnity insurance for 3½ years. This has not been "allowed" by the Authority. There was admittedly a long period (for about 2 years) of inactivity on the Authority's part. But I do not regard this as permission to the Applicant to carry on the regulated activities without PII cover. The correspondence makes it clear that from mid-2002 onwards the Authority have been actively expressing concern about the level of cover in an attempt to put right the Applicant's inadequacy of resources.

12. Mr Morfee, representing the Applicant, stressed that there was no hurry to implement the notice. No action had been taken for three years, and if the matter were so urgent, the Authority could have acted more speedily. He pointed to a Press Release of the Authority dated 3 February 2003. This addresses the problems presented by the difficulties within the industry of obtaining PII cover. It contains the following passage:

"8. If a personal investment firm does not have PII cover, or has non-compliant cover, we will consider its financial position, the nature of any PII cover it has, its PII claims records, and its past business mix. If overall, we are satisfied that the personal investment firm has adequate resources, we may give it a waiver (provided the requirements of section 148 of FSMA are met) from the requirement to have PII if it does not have cover, or issue additional guidance if it has non-compliant cover. This means that the personal investment firm is able to cover trading provided that it complies with some additional reporting requirements relating to customer complaints etc and has adequate cover to meet an increase to capital

requirement.”

Bearing in mind the practical impossibility of obtaining PII cover and the Applicant’s otherwise good record it should, Mr Morfee said, be possible for the Authority to modify the requirements imposed on the Applicant and people in the same position. There has, he argued, been a lack of flexibility in the Authority’s approach to the Applicant’s circumstances. It must in all the circumstances be possible to construct a framework within which the Applicant can trade without compliant PII cover. The result, Mr Morfee said, is that the decision to impose immediate effect on the notice is disproportionate and in violation of section 3.5.2 of ENF3.

13. Finally, our attention was drawn to a schedule of the assets of Mr Halfpenny and his wife. Mr Halfpenny it was said, had offered to make these assets available for any claims against his business.

14. Mr Greenhalgh for the Authority conceded that in the year 2002 firms in the financial services field have had difficulties in obtaining PII cover. That was the point of the Press Release. But Mr Halfpenny had been trading since 1999 without cover. The Authority had considered the proposal by Mr Halfpenny to make further funds available but had concluded that the amount was inadequate in the circumstances. It was not appropriate for a jointly owned house to be regarded as a resource for these purposes; here the house represented a very large proportion of the value of the joint assets of Mr and Mrs Halfpenny.

Conclusion

15. This is not a hearing of the reference. The question whether I should set aside the decision communicated in the Supervisory Notice does not strictly speaking arise. As it has been made with immediate effect, the question for me is whether that effect should be suspended to enable Mr Halfpenny to keep his regulated activities going while the reference proceeds to a hearing. In approaching this, it is appropriate to examine the circumstances leading to the issue of the Supervisory Notice. It is also appropriate to look at, without deciding, the Applicant’s case as to why the decision to issue the Notice was made in the first place. In this connection it is relevant to ask whether the Notice has come “out of the blue” or whether it has resulted from a fair amount of correspondence.

16. Of the facts leading to the decision the most significant is that the Applicant has traded for over three years without any PII cover and on present signs he will not get cover in the foreseeable future. He is therefore conducting a regulated activity without adequate resources and the Authority are bound to take action. The Authority know of the Applicant’s other assets. They have considered whether

they should modify the requirement for PII cover. Having addressed this issue the Authority have (admittedly after the Notice was served on the Applicant) concluded that the Applicant's assets are nonetheless inadequate.

17. I have read the correspondence between the Applicant and the Authority. The points taken in all the letters originating from the Applicant go to the same issue. This is that PII cover is not available; so why should the Authority vary the permission. Here, as I see it, the Authority have confronted that issue. It is, as they recognize, very tough on the firms in the Applicant's position. But there is a statutory obligation on the Authority to protect the public and consumers. Apart from that point I cannot see that the Applicant has put forward any other reason of substance as to why the Authority should allow him to continue to carry on the regulated activities without the imposition of conditions.

18. The only challenge that the Applicant has put forward to displace the Authority's decision to vary the position is, in essence, that he has a good record, without any actual claims being made good against him; and, as already noted, there are assets of his to meet the claims on the firm's business. Those features have been made known to the Authority which has nonetheless stuck to its decision to vary the permission. Nothing said on the Applicant's behalf indicates to me that he has any real chance of success were a full hearing of the reference to take place. There is no indication that suspending the effect of the Supervisory Notice will change the Applicant's position for the better or the worse with regard to the reference.

18. Taking all those factors into account I dismiss the Application.

STEPHEN OLIVER QC

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