Reference of refusal by F.S.A to approve applicants onus of proof – threshold conditions – fit and proper – non disclosure – prospect of prudent management.

THE FINANCIAL SERVICES AND MARKETS TRIBUNAL

Between

NORMAN DEAKIN

GWYNNETH ROE

IVAN HARRISON

RIDINGS GB

GLENBOW FINANCIAL MANAGEMENT LTD

Applicants

-and-

FINANCIAL SERVICES AUTHORITY

Respondent

Tribunal: **Mr T Gordon Coutts, QC (Chair)**
Mr Michael Hanson
Mr Andrew Lund

Sitting in Edinburgh on 2, 3, 6, 7 & 8 December 2004

MR B COCHRANE: **Appeared on behalf of the Applicants**

MR S GERRISH: **Appeared on behalf of the Respondent**

DECISION

Introductory

Decision notices were issued in these combined applications on 7 May 2004 in relation to the first four applicants, and in November 2004 in respect of the fifth (Glenbow). The applications were for part 5 approvals in respect of the individuals and part 4 authorisations in respect of the Companies. The Respondent refused all the applications for several reasons. These were, in respect of Ridings, that it could not satisfy the threshold conditions and in respect of the individuals that they could not satisfy the "fit and proper" test.

Onus or Burden of Proof

The Applicants in their Statement of Case and throughout appeared to be of the view that it was for the Respondent to prove their case i.e. to prove that the threshold conditions were not met, and to prove that the individuals were not fit or proper persons. Following that approach various legalistic points were made throughout the Hearing directed towards the burden of proof.

The Authority, it was submitted, did not have to prove that the threshold conditions were not met or that the Applicants were not fit and proper.

The Authority submitted that it required to show that the Tribunal could not be satisfied that the threshold conditions were met or that the particular candidate was fit and proper. It seemed to us that the Authority was thus accepting a burden in this case, which was not appropriate. It could and did lead to an unnecessary expenditure of time and a voluminous deployment of written material and evidence. They were in error in so doing.

The matter of burden of proof has been the subject of some discussion, perhaps obiter, in the application of David Thomas against the Authority on 23 July 2004. At paragraph 102 the Tribunal there said "the Tribunal will reach its decision on the evidence on argument presented to it and the burden of proof will be on the Respondent to show that on that evidence the Tribunal cannot be satisfied that the Applicant is fit and proper". That might appear to be in conflict with a view expressed in R V Maidstone Crown Court ex parte Olsen, The Times 21 May 1992 that the onus of establishing on the balance of probabilities that a licensee was a fit and proper person was on the Applicant. It has to be noted, however, that in Thomas the Authority was withdrawing or revoking an approval already in place, not determining a new application. In that case the status quo ante was being altered. In the present case it is not. Paragraph 102 in Thomas in our opinion requires to be confined to a case on the same facts.

It may be that this type of discussion caused the confusion in the mind of the Applicants and, further, caused unnecessary elaboration on the part of the Authority. It does not seem to this Tribunal that in the context of the Act it is correct to suggest that there is any onus on the Respondent or any burden of proof on them to establish anything in relation to the grant of approval or authorisation. Since the Tribunal replaces the Authority in decision making it is for the Tribunal to be satisfied on the evidence in front of it whether the threshold conditions are met and whether the Applicant or Applicants are fit and proper persons. The matter can be tested on the hypothesis that one side or the other leads no evidence. Since the applicants are seeking permission to operate in a regulated regime and require to show that they should be given such permission it appears to this Tribunal that the onus in this reference rests entirely on them. As a matter of convenience the Authority may lead at the Hearing and set out, as is right and proper, all the factors which they have had placed before them. But it is not what the Authority makes of those matters but what the Tribunal decides that is relevant in the context of the reference and it would be well, it is considered, for the future if Applicants realise that that they have got to persuade the Tribunal that they should be given the requisite authorisation and permission and not otherwise. Even a finding that the authority made some error of fact would not

necessarily lead to a direction that the application be granted without evidence from the Applicants, written or oral.

Background facts prior to application

We find that the following matters occurred prior to the applications with which we are concerned being made. The matters were canvassed before the Authority and ourselves and although some doubt was expressed about the relevance of some of them we hold that the Authority were entitled to have consideration to any such facts, for what they were worth, as indeed was the Tribunal.

Mr Deakin, the key figure in this whole affair, began his business life as a salesman. He transferred in about 1977 to Pearl Assurance where he acted as Section Manager. He thereafter acted as a Manager until 1995 when his duties (with Frizzell Financial Management) included training, compliance and development matters. In 1997 he was an Associate Director of Bowland Financial Management Ltd and claimed to have duties providing independent financial advice for a high net worth client group. In 1999-2000 4 companies were incorporated; MBA Sterling Direct Ltd, Sterling GB Ltd, Sterling GB Direct Ltd and MBA Sterling (UK) Ltd. Mr Deakin was a director of each of these companies.

On 2 August 2000 by resolution Sterling GB Direct Ltd changed its name to MBA Sterling Direct Ltd and the former MBA Sterling Direct Ltd changed its name to Sterling GB Direct Ltd. No explanation which sounded plausible to the Tribunal was given for this reshuffle. It has caused confusion to customers, creditors and regulators for which the directors of those companies must bear any blame.

Mr Deakin claimed to be responsible for training and compliance issues with Sterling GB Direct Ltd from 2000 onwards. Apart from the now MBA Sterling Direct Ltd all the other companies are in liquidation, Sterling GB Ltd and Sterling GB Direct Ltd by 28 November 2003.

The business carried out by Sterling GB Direct

This consisted of the selling of small value life assurance policies round the houses. The scheme whereby these policies were sold to the public appeared to be, in essence, the provision by a firm, “Shopacheck”, of a loan to cover the annual premiums. In the event of the weekly payments of that loan not being met Shopacheck cancelled the policy and reclaimed the premium paid by offset against other premiums due. Sterling Direct became aware that Shopacheck were not paying sufficient funds into the account designed to meet the premiums to the insurers and Sterling

GB supported that account to a substantial level. Due to inadequate monitoring and supervision of these transactions, which were many, in particular, losses to Sterling GB Direct which, because of internal arrangements, also affected Sterling GB. The result for the consumer was the failure of the policy, loss of protection and a loan debt.

Ridings GB Limited

Shortly after the above liquidations the firm Ridings was incorporated. The directors at incorporation were the Applicants Gwynneth Roe and Ivan Harrison who were the only, equal, shareholders and also provided loan finance. The Tribunal had no doubt, however, that Mr Deakin was the driving force behind the new company which was intended to continue the insurance business previously carried on by the Sterling entities and to, possibly, succeed to trail commissions. Mrs Roe and Mr Harrison had been employees of the companies controlled by Mr Deakin. They had never been directors of any company.

The current applications

Ridings applied to the Authority for authorisation and the 3 individual applicants for approval. Mr Deakin became a director of Ridings in 2004, partly in response to the Authority not being

persuaded of the competence and fitness of the directors Roe and Harrison to perform controlled functions.

Because the Authority had not been minded to approve the 3 individual applicants, as an interim measure Ridings GB Limited became an Appointed Representative of Glenbow Financial Management, a company in which Mr Cochrane, who represented the Applicants before and at the Tribunal hearing, has a material interest. Glenbow sought approval for Mr Deakin to perform controlled function CF1(AR) as well as CF21 in respect of Ridings Limited.

It appeared in the course of the hearing that Ridings had been operating as an approved representative of Glenbow Financial Management without an approved person in the CF1(AR) Director controlled function and was therefore in breach of the Act. It was suggested by Mr Deakin that they were so operating as a result of advice from the firm IFA Compliance Ltd.

The applications

We could see from the evidence that, from the date of the applications until the ultimate refusal, the Authority went to great efforts to determine whether they could approve the applications. Much correspondence and also meetings took place when the

Authority became concerned about the propriety of the Applicants. We find that the Applicants had ample opportunity to explain, if they could, and to give reasons why their Applications should be granted. We find that they failed to do so before the Authority and equally before us. It is necessary to outline the concerns and the reasons therefor and to make findings in relation thereto.

Evidence at the Hearing

The Tribunal heard evidence from Mr Hillier, Miss Jordan and Mr Cooper all officers of the Respondent; also from Mr Fotherby and Ms Linnegan both former employees in the Sterling Companies. They heard evidence from the Applicants Mr Deakin, Mrs Roe and Mr Harrison. The procedure adopted was that each of these witnesses prepared a statement which was taken as Evidence in Chief and each was subject to cross-examination. Other written statements to which the Tribunal was invited to have regard were those of Mr Drainer and Mr Thomas of the Authority in relation to the Glenbow application. There was also produced and no objection taken to the statement of Mr Bennett, who wrote in support of Mr Deakin.

The Tribunal saw no reason to doubt the reliability and credibility of the Authority's officers. They regarded Mr Harrison as doing his best to tell the truth in an unfortunate situation. They had

reservations about the evidence of Ms Linnegan on the historical matters relating to the Sterling entities. Her role and activities in the matters put before us was not entirely clear. They were not inclined unless independently supported to accept the evidence of Mr Deakin. As an example in his written statement, confirmed on oath, Mr Deakin alleged that, without his knowledge or consent or sight of minutes, in 2002 Ms Linnegan had had her wages increased. When that was put in cross-examination to her she produced and referred to a letter (PAL8) dated 8 May 2002 admittedly signed by Mr Deakin which contradicted his statement as follows:

> *"Following the recent review of duties and responsibilities within Sterling GB and Sterling GB Direct Ltd I am pleased to inform you on behalf of the board that your salary has been increased to £20,000 per annum with effect from 1 May 2002".*

With regard to Mrs Roe they regarded her evidence when given in the Tribunal room as corroborating the Respondents view of her inadequacies and inability to understand or to perform the function of a Director let alone any controlled function. She was wholly out of her depth.

Necessary requirements for approval and authorisation

These matters are explained at length in the Authority's statutory regime. In Schedule 6 of the Act threshold conditions are provided. Four relevant conditions were canvassed before the Tribunal specifically in relation to Ridings, and five in relation to the individuals, and also as impacting on the application by Glenbow for approval of Mr Deakin performing controlled functions.

Schedule 6 provides *inter alia*

… 4 Adequate resources

(1) The resources of the person concerned must, in the opinion of the Authority, be adequate in relation to the regulated activities that he seeks to carry on, or carries on.

(2) In reaching that opinion, the Authority may-

(a) take into account the person's membership of a group and any effect which that membership may have; and
(b) have regard to-

(i) the provision he makes and, if he is a member of a group, which other members of the group make in respect of liabilities (including contingent and future liabilities); and
(ii) the means by which he manages and, if he is a member of a group, which other members of the group manage the incidence of risk in connection with his business.

5. Suitability

The person concerned must satisfy the Authority that he is a fit and proper person having regard to all the circumstances, including-

(a) his connection with any person;

(b) the nature of any regulated activity that he carries on or seeks to carry on; and
(c) the need to ensure that his affairs are conducted soundly and prudently.

"Adequate resources" we were told was (and in our opinion should be) interpreted broadly to include both financial and human resources and any other relevant factors. It is necessary to determine whether the firm will satisfy and continue to satisfy threshold condition 5 and all relevant factors may be taken into account to the extent that they are significant. Such relevant matters include but are not limited to whether a firm:

(a) Conducts, or will conduct, its business with integrity and in compliance with proper standards;

(b) Has, or will have, a competent and prudent management; and

(c) Can demonstrate that it conducts, or will conduct its affairs with the exercise of due skill care and diligence. (COND 2.5.4 G(2)).

and may include but are not limited to whether:

The firm has been open and co-operative in all of its dealing with the FSA and any other regulatory body (see Principle 11 (Regulations with regulators)) and is *ready, willing and*

organized to comply with the requirements and standards under the regulatory system and other legal, regulatory and professional obligations; the relevant requirements and standards will depend upon the circumstances of each case

…

and the firm has taken reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system that apply to the firm and the regulated activities for which it has, or will have, permission. (COND 2.5.6 G).

Further in terms of principle 11 a firm must deal with its regulators in an open and co-operative way, and must disclose to the FSA appropriately anything relating to the firm of which the FSA would reasonably expect notice.

Further a firm must notify the FSA if civil proceedings were brought against it and the amount of the claim is significant in relation to the firms financial resources or its reputation. It must take reasonable steps to ensure that all the information it gives to the FSA in accordance with the Rule in any part of the Handbook is factually accurate or in the case of estimates and judgments, fairly and properly based after appropriate enquiries have been made by

the firm; and also complete in that is should include anything of which the FSA would reasonably expect notice.

In respect of this guidance in relation to Ridings the Authority's concerns were:

(i) That the governing body is not made up of individuals with the appropriate range of skills and experience: Mr Deakin may have experience, but there are concerns as to his level of skill based on:

(a) Previous conduct in relation to Sterling GB and Sterling Direct;

(b) Conduct in relation to the Ridings application.

It was submitted that if one excludes Mr Deakin from the governing body, Mr Harrison and Mrs Roe do not have sufficient experience or skill. This it was said was further evidenced by the conduct of Sterling with respect to the Authority, whilst Mr Deakin was away from work at Sterling due to ill-health.

Part 4 Approval

It was submitted by the Authority that:

1) The proposed structure of the governing body of Ridings, with the inclusion of two previous employees of Mr Deakin as CF1 status does not give the Authority confidence that Mrs Roe and Mr Harrison will have sufficient authority or the ability effectively to challenge Mr Deakin.

2) The proposed structure in respect of Ridings (AR) that only Mr Deakin would be applying for CF1 (AR) approval raises concerns as to the reason for the ownership of Ridings by Mrs Roe and Mr Harrison; and their role within that firm.

3) The firm has not demonstrated to the Authority that it has made arrangements to put into place an adequate system of internal control to comply with the requirements and standards under the regulatory system (see SYSC 3.1 (Systems and Controls)).

4) The firm has not approached the control of financial and other risks in a prudent manner:

(a) in respect of its proposed business plan;

(b) in respect of demonstrating contracts, letters of agreement or similar in relation to a significant anticipated income stream;

(c) in respect of demonstrating adequate prudence or compliance with the rules, for example relating to professional indemnity insurance;

(d) or by updating the information, for example financial forecasts to reflect modifications in the firm's proposals;

(e) in respect of demonstrating how the problems that arose due to failures at Sterling GB and Sterling Direct would be avoided in the future.

5) There is an additional burden in respect of Ridings, in that Mr Deakin had been a director of Sterling entities that went into liquidation, with substantial debts in circumstances that suggest there was no good reason for the liquidation of Sterling GB, were it not for the confused relationship between CGNU, Shopacheck, Sterling GB and Sterling Direct. Further that it is immaterial that it is alleged that the reason for the liquidation of Sterling Direct is that it was due to the inadequacies of Cattles/Shopacheck (which in any event is not demonstrated).

6) Ridings has not provided any evidence that it will not be posing an unacceptable risk to consumers, having especial regard to the background of the liquidation of Sterling GB and Sterling Direct.

Part 5 Approval

It is appropriate in considering whether a person is fit and proper to have regard to Section 61 of the Act which provides:

"the Authority may have regard (amongst other things) to whether the candidate …

(a) has obtained a qualification;
(b) has undergone, or is undergoing training;
(c) or possesses a level of competence,

required by the general rules …"

In the published FIT module of the handbook the following advice and guidance has been promulgated:

FIT 1.1.2 G "The purpose of FIT is to set out and describe the criteria that the FSA will consider when assessing the fitness and propriety of a candidate [that is an applicant for approval] for a controlled function (see generally SUP 10 on approved persons)…"

FIT 1.3.1 G "The FSA will have regard to a number of factors when assessing the fitness and propriety of a person to perform a

particular controlled function. The most important considerations will be a persons:

(i) Honesty, integrity and reputation

(ii) Competence and capability; and

(iii) Financial soundness."

FIT 1.3.2 G "In assessing fitness and propriety, the FSA will also take into account the activities of the firm for which the controlled function is or is to be performed, the permission held by that firm and the markets within which it operates".

FIT 1.3.3 G "The criteria listed in FIT 2.1 to FIT 2.3 are guidance and will be applied in general terms when the FSA is determining a person's fitness and propriety. It would be impossible to produce a definitive list of all the matters which would be relevant to a particular determination."

FIT 2.1.1 G "In determining a person's honesty, integrity, and reputation, the FSA will have regard to matters including, but not limited to, those set out in FIT 2.1.3. The FSA should be informed of these matters (see SUP 10.13.16), but will consider the circumstances only where relevant to the requirements and standards of the regulatory system. For example under FIT 2.1.3

G(1), conviction for a criminal offence will not automatically mean an application will be rejected. The FSA treats each candidate's application on a case-by-case basis, taking into account the seriousness of, and the circumstances surrounding the offence, the explanation offered by the convicted person, the relevance of the offence to the proposed role, the passage of time since the offence was committed and evidence of the individual's rehabilitation".

FIT 2.1.3 "The matters referred to in FIT 2.1.1 G to which the FSA will have regard include, but are not limited to …

> (9) whether the person has been a director… of a business that has gone into… liquidation… while the person has been connected with that organisation…
>
> (13) whether in the past the person has been candid and truthful in all his dealings with any regulatory body and whether a person demonstrates a readiness and willingness to comply with the requirements and standards of the regulatory system and with other legal, regulatory and professional requirements and standards."

FIT 2.2.1 G "In determining a person's competence and capability, the FSA will regard to matters including but not limited to:

(1) whether a person satisfies the relevant requirements of the FSA's Training and Competence sourcebook (TC) in relation to the controlled function the person performs or is intended to perform;

(2) whether the person has demonstrated by experience and training that the person is able, or will be able if approved, to perform the controlled function".

The Authority purported to apply these principles in refusing to give approval of authorisation. It is for the Tribunal to consider afresh whether it has been demonstrated that approval and authorisation should be given. On the evidence not one of the conditions above quoted has been demonstrated to the Tribunals satisfaction as being or being about to be satisfied. In relation to the particular matter canvassed our findings are set out below.

In relation to the liquidation of the Sterling Companies, that was a matter which, plainly, required to be disclosed and explained. Some effort seems to have been made to give information to the Authority with which they were not satisfied. The opportunity was therefore present for the applicants to satisfy the Tribunal that the

liquidation of the Sterling Companies was not a matter which impacted adversely upon the applications. In the Tribunal's view this was not done. It is sufficient to dispose of the matter of the history of the Sterling Companies to conclude that whatever the reason for the confused and confusing court procedures which ensued whether that be because of changes of name, because of inadequate accounting, inadequate supervision or some similar cause it required to be demonstrated to us that those responsible, and in this instance Mr Deakin, did exercise or see to it that there was exercised sufficient accounting and other information to avoid the situation which arose. It may well be that that was the situation which arose because of the practice of lending the insured money to pay a premium which was then collected back from the insured by way of a loan payment, default in which would avoid the policy, was at the root of the difficulty. The Authority had rightly and the Tribunal have serious reservations about such a system operating in a way which adequately protected the public. Perhaps it might, but it was not demonstrated to us that it could. That circumstance must underlie any matter in which Mr Deakin is involved.

The factors were compounded by what was accepted to be a totally inadequate business plan provided to the Authority and to the Tribunal. It was conceded to be inadequate but no effort was made to provide the Tribunal with anything which approached adequacy.

It was a mere repetition of the previously failed business plan applying to the Sterling and Shopacheck operations. That circumstance also demonstrates an inadequate realisation of what is required for the purposes of the regulatory regime.

Further to the problem with the business plan was the lack of any other compelling evidence that Ridings was an entity which had taken reasonable steps to identify and measure any risks of regulatory concern. We find that it failed to have installed or to set in motion provision for installing appropriate systems and controls and did not have appropriate personnel. In the course of the Hearing it was claimed by Mr Cochrane and Mr Deakin that it had no longer intended that Ridings would undertake such business and that it would simply operate as an IFA. This assertion was directly contradicted by the evidence presented, and by the testimony of Mr Harrison. It follows that as matters stand Ridings cannot in any event be given authorisation since they will not have persons in place who can perform the necessary controlled functions.

Further there was no satisfactory evidence that there was, or could be in place satisfactory Personal Indemnity Insurance.

The Tribunal, like the Authority, did not accept that Ridings was anything other than a cover for Mr Deakin's involvement in

matters which require to be regulated. The appointment of Mrs Roe and Mr Harrison as Directors and their having been involved in the provision of capital did not save the situation. It was plain from the evidence in the correspondence with and interviews given to the Authority that Ridings could not operate without Mr Deakin pulling the strings and his credibility was not enhanced by the story that he wished to take a back seat after the debacle at Sterling. Ultimately when it was demonstrated that neither Mrs Roe nor Mr Harrison were equipped to exercise the necessary controlled functions to enable the company to operate, application was made to approve Mr Deakin to do so. but that merely serves to raise further questions about the entire set-up and structure of Ridings and the involvement of Mr Deakin.

In relation to Glenbow it appeared that the advice given about permitting Ridings to operate as an appointed representative without an approved person holding the CF1(AR) function was unsound. Although Ridings being an appointed rep would overcome the difficulties of approval, the failure was in not having a CF1(AR) in place. An appointed representative must have a person responsible for this controlled function. There are none such at Ridings.

Conclusion

Since none of the above concerns have been met to the satisfaction of the Authority nor subsequently to the Tribunal each and every one of the applications requires to be refused.

We would however wish to refer to a matter which arose in the course of the Applicants dealings with the Authority. A letter was sent by Kirsty Brown of the Authority on 30 July 2003 which indicated that approval would be recommended by her if certain financial conditions were met. Very shortly thereafter other matters were brought to her attention. The Applicants sought to found on that letter. They are not entitled to do so.

A meeting was called by the Authority. Minutes were kept. The Applicants were not provided with a copy because they did not ask for one. Dispute arose about the narration of the conduct of and statements at that meeting. The minutes were said to be faulty by the Applicants and in particular by Mrs Roe. In the event we had no hesitation in accepting the minutes produced as accurate from the evidence about them from the Authority and Ms Jordan and in rejecting that of Mrs Roe challenging the minutes produced to us. However it seems to us that such a meeting which was attended with some degree of formality would have been better with a formal agenda and minutes circulated. Not every meeting between the Authority and an Applicant would require such formality but in this

instance, and particularly in light of the letter of 30 July 2003 that would have been better practice for all concerned, and assisted any Tribunal. When appropriate, in future, that procedure should be followed.

T GORDON COUTTS, QC

CHAIRMAN

RELEASE: 8 FEBRUARY 2005