

## At the FSA last week

### FSA fines HSBC £10.5 million in relation to asset backed investment products

In the latest of a string of similarly significant fines imposed against major institutions in respect of historic sales of investment products, the FSA has imposed a financial penalty of £10.5 million on HSBC. The penalty relates to breaches of Principle 9 (Customers: relationships of trust) of the FSA's Principles for Businesses (and associated breaches of historic and current conduct of business rules) arising from sales of asset backed investment products by a subsidiary acquired by HSBC in 2005.

The penalty, the level of which reflected HSBC's significant co-operation throughout the FSA's investigation, was reduced from £15 million under the FSA's executive settlement procedures.

### Key issues

- FSA fines HSBC £10.5 million in relation to asset backed investment products
- Judicial review challenge to FSA's publication of Decision Notice dropped
- Court of Appeal upholds FSA action to wind up satellite "warranty" providers
- Insider dealing trial commences

Specifically, the FSA found that HSBC

- failed to ensure that the products offered to customers were suitable in view of their life expectancy, attitude to risk or tax status;
- failed to ensure that investments and savings plans were adequately diversified, or that sufficient amounts of funds were available to customers on deposit;
- failed to ensure that suitability letters issued to customers were appropriately tailored, accurate, balanced or up-to-date

In addition to co-operating fully with the FSA, HSBC has commenced a comprehensive review process which will lead to customer redress being paid in appropriate cases.

[http://www.fsa.gov.uk/pubs/final/hsbc\\_2dec11.pdf](http://www.fsa.gov.uk/pubs/final/hsbc_2dec11.pdf)

### FSA sets out intention to ban "death bonds"

In the latest example of the practical application of its product intervention strategy, the FSA has issued a guidance consultation paper (GC11/28) in relation to traded life policy investments ("TLPs"). TLPs, also known as "traded life settlements", "senior life settlements" or "death bonds", are products which invest in US life insurance policies, and which effectively "bet" on the date of death of particular sets of policyholders.

This guidance is much briefer than that issued to date by the FSA in respect of other types of products as part of its product intervention

strategy. However, it is the clearest and most unequivocal yet.

Previously, the FSA has issued guidance as to the steps which firms should take to ensure that consumers' interests are safeguarded throughout the design, distribution and sales processes for payment protection products and structured products, but has not until now indicated that a particular type of product should not reach the market at all.

Although the guidance itself does not impose a ban, it goes as far as the FSA is currently empowered to go in respect of TLPs, which it describes as "completely unsuitable" for the majority of UK consumers and which it states, in no uncertain terms, should not be promoted or sold to UK retail investors.

The FSA's misgivings in relation to TLPs are not based on moral objections to betting on the date of death of sections of the American population, but rather on the complexity of the products and its perception of the associated risk posed to UK retail investors. Specifically, the FSA guidance paper identifies the risks arising from the inherently imprecise science of calculating life expectancy, the illiquid nature of the investments, the fact that both the assets themselves and often the firms selling them are located offshore and problems with sales practice (including some references to similarities to "Ponzi" style arrangements where yields to previous investors are dependent upon receipts from new investors).

The FSA's clear intention is to ban TLPs altogether as soon as possible.

The press release accompanying the issuing of the guidance indicates that consultation on such a move will take place next year. In the meantime, consultation with other European regulators continues with the aim of agreeing a strategy, using regulators' current powers, together with those which they will receive under developments such as the ongoing review of MiFID, to enable pan-European bans of products deemed to be "toxic" (such as TLPs).

The FSA's enthusiasm for such measures appears to be matched at the supranational European level. For example (although he did not refer specifically to TLPs), Steven Maijor, Chairman of ESMA, last week set out his wish to use powers proposed under the ongoing MiFID review to ban "faulty" products from the European retail market (albeit that he acknowledged that bans imposed by ESMA under the terms of MiFID as revised could only be temporary in nature, and that permanent bans would be the province of national authorities<sup>1</sup>).

In common with the guidance issued by the FSA in relation to payment protection and structured products as part of its product intervention strategy, this latest guidance in relation to TLPs is born largely of significant and high profile instances of consumer detriment. In this instance, the consultation, and the stated intention to ban TLPs in due

course, is based largely on the experience of dealing with the collapse in 2009 of Keydata, whose portfolio contained a large number of these products. Moves towards increasingly intrusive and earlier intervention by the FSA (and indeed other national and European regulators) are aimed at preventing, rather than reacting to, any future recurrence of similar problems.

Firms are invited to comment on the contents of the consultation paper by 23 January 2012.

[http://www.fsa.gov.uk/pubs/guidance/gc11\\_28.pdf](http://www.fsa.gov.uk/pubs/guidance/gc11_28.pdf)

### Judicial review challenge to FSA's publication of Decision Notice dropped

The subjects of the first Decision Notice to be published by the FSA have dropped their judicial review challenge to the FSA's decision to publish that notice.

The FSA is pursuing the Canadian trading platform previously known as Swift Trade Inc ("**Swift Trade**") (subsequently known as 7722656 Canada Inc ("**Canada Inc**") until the voluntary dissolution of that company in December 2010) for alleged market abuse.

The Decision Notice ([http://www.fsa.gov.uk/pubs/final/swift\\_trade.pdf](http://www.fsa.gov.uk/pubs/final/swift_trade.pdf)) was published in August 2011 following unsuccessful attempts by Swift Trade and its former Chief Executive Officer Peter Beck, who it also names, to persuade first the High Court to grant an injunction and subsequently the Upper Tribunal to give directions restraining publication. After the failure of those efforts and the publication by the FSA of the Decision Notice, Swift Trade and Mr Beck commenced judicial review

proceedings, which have now been discontinued by consent.

The Decision Notice remains the most significant to be published since the extension (in October 2010) of the FSA's powers enabling it to publish such notices under section 391 FSMA. It alleges a systematic campaign of "layering" by Swift Trade to manipulate the price of various shares listed on the London Stock Exchange. The FSA proposes a financial penalty of £8 million.

Swift Trade and Mr Beck have challenged the FSA's findings and proposed penalty set out in the Decision Notice. If the Upper Tribunal agrees with the FSA's findings and proposed penalty, the fine imposed will be the largest in a contested market abuse case in the UK. Hearings before the Upper Tribunal are scheduled to take place in June 2012.

[http://www.fsa.gov.uk/pages/Library/Communication/Statements/2011/swift\\_trade.shtml](http://www.fsa.gov.uk/pages/Library/Communication/Statements/2011/swift_trade.shtml)

### Court of Appeal upholds FSA action to wind up satellite "warranty" providers

Action taken by the FSA to wind up two businesses for carrying out unauthorised business has been upheld by the Court of Appeal. The FSA took action against Digital Satellite Warranty Cover Limited ("**DWSC**") and Bernard Freeman and Michael Sullivan, trading as Satellite Services in January 2011, securing winding up orders in respect of both. Both firms appealed against the winding up orders. These appeals have now been dismissed.

<sup>1</sup> Speech by Steven Maijor at EFAMA Investment Management Forum, 29 November 2011 - <http://www.esma.europa.eu/popup2.php?id=8097>

The action was based upon the cover provided by both businesses for repairs to satellite equipment. The FSA argued, and the Court has held, that the product described by these businesses as an "extended warranty" was in fact a contract of insurance and, as such, required them to be authorised by the FSA.

<http://www.fsa.gov.uk/pages/Library/Communication/PR/2011/103.shtml>

### Insider dealing trial commences

The trial of former management consultant Rupinder Sidhu, accused of 23 counts of insider dealing in 2008 and 2009 and one count of money laundering of the proceeds of that activity, has commenced at Southwark Crown Court. Mr Sidhu is alleged, together with former trader Anjam Ahmad, to have executed numerous spread bets based upon inappropriate exchanges of information.

However, Mr Sidhu stands trial alone following a deal negotiated between the FSA and Mr Ahmad and approved by the Court in June 2010. Further to the first use by the FSA of its powers under Serious Organised Crime and Police Act 2005 to enter into plea agreements in return for assistance from defendants, Mr Ahmad, having pleaded guilty to similar offences to those of which Mr Sidhu is accused, received a suspended sentence, was required to complete 300 hours of community service and was fined £50,000. A confiscation order of £106,280 was also imposed and, in separate action, a Final Notice issued to him by the FSA required disgorgement of the profits of regulatory misconduct related to the matters in respect of which he

pleaded guilty (which totalled an additional £131,000).

Mr Sidhu's trial continues and is expected to last several months.

### Other Final Notices

In a Final Notice dated 4 November 2011 but released last week, the FSA has imposed a financial penalty of £49,000 (reduced from £70,000 for early settlement) on **Julian Harris**, has withdrawn his CF10 (compliance oversight) approval, and has prohibited him from carrying out that or any other compliance oversight related function. The action relates to his having been "knowingly concerned" in breaches of Principle 3 (management and control) of the FSA's Principles for Businesses by Julian Harris Financial Consultants and Julian Harris Mortgages Limited in relation to the vetting and compliance monitoring of appointed representatives of those firms.

<http://www.fsa.gov.uk/pubs/final/julian-harris.pdf>

The FSA has cancelled the Part IV permission of **PBF Financial Limited (in liquidation)**, as it is unable to meet its liabilities as they fall due.

[http://www.fsa.gov.uk/pubs/final/pbf\\_financial\\_limited.pdf](http://www.fsa.gov.uk/pubs/final/pbf_financial_limited.pdf)

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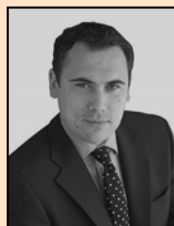
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