Financial Services Authority

FINAL NOTICE

To: **David Connor Redmond**

Individual Reference Number: **DCR01063**

Date: **18 May 2009**

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("the FSA") gives you final notice that it has taken the following action:

1 THE ACTION

1.1 The FSA has given Mr David Redmond ("Mr Redmond") a Decision Notice which notified Mr Redmond that, pursuant to section 56 of the Financial Services and Markets Act 2000 ("the Act"), the FSA had decided to impose on him a prohibition order prohibiting him from performing any function in relation to any regulated activity carried on by any authorised or exempt person or exempt professional firm.

1.2 Mr Redmond has confirmed that he will not be referring the matter to the Financial Services and Markets Tribunal.

1.3 Accordingly, for the reasons set out below and having agreed with Mr Redmond the facts and matters relied on, the FSA imposes a prohibition order on Mr Redmond in these terms.

1.4 The prohibition order has effect on 20 May 2009. The FSA is minded to revoke the prohibition order, on Mr Redmond's application, at any time after two years from the date of the Final Notice, in the absence of new evidence that Mr Redmond is not fit and proper.

2 REASONS FOR THE ACTION

Summary

2.1 This notice is issued to Mr Redmond in the light of his conduct on 6 and 7 February 2008.

2.2 Mr Redmond was at the relevant time a trader on the Freight Desk of Morgan Stanley's Commodities Division in London. His role involved both freight and oil trading. Mr Redmond was approved, under section 59 of the Act, to perform the CF30 'Customer' Controlled Function at Morgan Stanley. However, at the relevant time he carried out proprietary trading rather than trading for customer accounts.

2.3 Mr Redmond is no longer employed by Morgan Stanley and is not currently an approved person. The FSA makes no criticism of Morgan Stanley or any individuals other than Mr Redmond in relation to the matters set out in this notice.

2.4 Between 17.04 and 19.37 on 6 February 2008, Mr Redmond sold 24,868 lots[1] and bought 19,493 lots of WTI Futures on the ICE Futures (Europe) ("ICE") web-based trading platform, WebICE. By 19.37, Mr Redmond had a substantial net short position of 5,395 lots[2].

2.5 At 20.04 on 6 February 2008, Mr Redmond transferred 5,400 lots of WTI Futures from his own strategy (account) to the strategy of one of his colleagues through a series of inter-strategy trades. Mr Redmond did this to try to conceal the substantial short position in WTI Futures, and did so without his colleague's knowledge.

2.6 At 20.08 on 6 February 2008, Mr Redmond submitted the Freight Desk's daily profit and loss report ("the P&L report") into Morgan Stanley's risk management system, which he was required to do. Given the inter-strategy trades he had made at 20.04, the P&L report did not reflect the substantial short position. Mr Redmond then reversed the transfer and transferred the position back from his colleague's strategy to his own strategy by way of a further series of inter-strategy trades.

2.7 Mr Redmond left the office that evening without informing or attempting to inform his managers about the substantial short position he had created. Instead, by making the inter-strategy trades to his colleague's strategy before submitting the P&L report, Mr Redmond sought to conceal the short position from Morgan Stanley, thereby exposing the firm to the risk of incurring a significant loss. On 6 February 2008, the price in WTI Futures fluctuated by more than $2, although in the two and a half hour period in which Mr Redmond traded, the price was relatively stable and Mr Redmond traded within a price range of $0.78. Using $2 as a benchmark (and the price could have moved outside this range), the substantial short position of 5,395 lots equates to an exposure to a possible loss of approximately $10 million.

2.8 By 13.56 on 7 February 2008, Mr Redmond had bought back sufficient lots of WTI Futures to close the substantial short position. Mr Redmond still had not informed or attempted to inform his managers about that position or his attempt to trade out of it, despite having had opportunities to do so. When he discovered shortly after 14.00 on 7 February that Morgan Stanley was investigating his trading, Mr Redmond informed his

[1] One lot is equivalent to 1,000 barrels

[2] Mr Redmond already had a net short position of 20 lots as at 17.04

manager that he had made an error and ended up with a large short position overnight which he had since traded out of. Mr Redmond did not admit to the inter-strategy trades to his colleague's strategy until directly challenged about this.

2.9 Mr Redmond was unable to provide a satisfactory explanation for his trading on 6 and 7 February 2008. His trading and his failure to report it was in breach of Morgan Stanley's policies and procedures. Mr Redmond was suspended from Morgan Stanley on 7 February 2008 and was subsequently dismissed for gross misconduct on 10 March 2008. Mr Redmond ceased to be an approved person on 6 March 2008.

2.10 The FSA finds that, as a result of his conduct on 6 and 7 February 2008, Mr Redmond is not a fit and proper person to perform functions in relation to a regulated activity carried on by any authorised person, exempt person or exempt professional person. The FSA has made an order prohibiting Mr Redmond from performing functions in relation to a regulated activity carried on by any authorised person, exempt person or exempt professional person.

2.11 Whilst the FSA believes that a prohibition order is necessary and proportionate in order to achieve the FSA's regulatory objective of market confidence, and to deter Mr Redmond and others from similar conduct, the FSA would be minded in all the circumstances to revoke the prohibition order after two years from the date of the Final Notice, upon application by Mr Redmond, in the absence of new evidence that Mr Redmond is not fit and proper.

Relevant Statutory and Regulatory Provisions

2.12 The FSA considers that taking this action against Mr Redmond helps it achieve its regulatory objective, as set out in section 2(2) of the Act, of maintaining market confidence in the financial system.

2.13 The FSA has the power, pursuant to section 56 of the Act, to make an order prohibiting an individual from performing a specified function, any function falling within a specified description, or any function, if it appears to the FSA that that individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by any authorised person, exempt person or exempt professional person.

Relevant Guidance

2.14 In making a prohibition order against Mr Redmond, the FSA has had regard to guidance published in the FSA Handbook.

<u>Fit and Proper Test for Approved Persons</u>

2.15 The part of the FSA Handbook entitled The Fit and Proper Test for Approved Persons ("FIT") sets out guidance on how the FSA will assess the fitness and propriety of a person to perform a particular controlled function.

2.16 The purpose of FIT is to outline the main criteria the FSA will consider when assessing the fitness and propriety of a candidate for a controlled function. FIT is also relevant in assessing the continuing fitness and propriety of an approved person.

2.17 FIT 1.3.1G states that the FSA will have regard to a number of factors when assessing the fitness and propriety of a person and that the most important considerations will be the person’s honesty, integrity and reputation, competence and capability and financial soundness.

2.18 FIT 2.1.1G provides that, in determining a person’s honesty, integrity and reputation, the FSA will have regard to factors including, but not limited to, those set out in FIT 2.1.3G. FIT 2.1.3G sets out the following factors, amongst others, which are relevant to this matter:

(5) whether the person has contravened any of the requirements and standards of the regulatory system; and

(11) whether the person has been dismissed, or asked to resign and resigned, from employment.

2.19 Chapter 9 of the Enforcement Guide (“EG”) sets out the FSA's approach to exercising its power under section 56 of the Act to make prohibition orders.

2.20 EG 9.4 summarises the FSA’s policy on making prohibition orders. In particular:

“The FSA has the power to make a range of prohibition orders depending on the circumstances of each case and the range of regulated activities to which the individual’s lack of fitness and propriety is relevant. Depending on the circumstances of each case, the FSA may seek to prohibit individuals from performing any class of function in relation to any class of regulated activity, or it may limit the prohibition order to specific functions in relation to specific regulated activities. The FSA may also make an order prohibiting an individual from being employed by a particular firm, type of firm or any firm.”

2.21 EG 9.5 states:

“The scope of a prohibition order will depend on the range of functions which the individual concerned performs in relation to regulated activities, the reasons why he is not fit and proper and the severity of risk which he poses to consumers or the market generally.”

2.22 EG 9.6 states that, where the FSA issues a prohibition order, it may indicate in the final notice that it would be minded to revoke or vary the order on the application of the individual in a specified number of years in the future, in the absence of new evidence that the individual is not fit and proper. It states that this approach will only be adopted in cases where the FSA considers it appropriate in all the circumstances, taking into account factors such as at EG 9.9. It also states that, if an individual’s prohibition order is revoked, the individual would still have to satisfy the FSA as to his fitness for a particular role in relation to any future application for approval to perform a controlled function.

2.23 EG 9.9 states that, when it decides whether to exercise its power to make a prohibition order against an approved person, the FSA will consider all the relevant circumstances of the case. These may include, but are not limited to, factors such as:

(2) whether the individual is fit and proper to perform functions in relation to regulated activities. The criteria for assessing the fitness and propriety of approved persons are set out in FIT 2;

(3) whether and to what extent the approved person has failed to comply with the Statements of Principle issued by the FSA with respect to the conduct of approved persons;

(5) the relevance and materiality of any matters indicating unfitness;

(6) the length of time since the occurrence of any matters indicating unfitness;

(7) the particular controlled function the approved person is (or was) performing, the nature and activities of the firm concerned and the markets in which he operates;

(8) the severity of the risk which the individual poses to consumers and to confidence in the financial system; and

(9) the previous disciplinary record and general compliance history of the individual.

2.24 EG 9.11 states that due to the diverse nature of the activities and functions which the FSA regulates, it is not possible to produce a definitive list of matters which the FSA might take into account when considering whether an individual is not a fit and proper person to perform a controlled function.

2.25 EG 9.12 provides examples of types of behaviour which have previously resulted in the FSA deciding to issue prohibition orders. These include severe acts of dishonesty (EG 9.12(3)) and serious lack of competence (EG 9.12 (4)). EG 9.13 states that certain matters which do not fall squarely, or at all, within such types of behaviour may also fall to be considered.

2.26 EG 9.17 states that where the FSA is considering making a prohibition order against an individual other than an approved person, the FSA will consider the severity of the risk posed by the individual, and may prohibit the individual where it considers this is appropriate to achieve one or more of its regulatory objectives. EG 9.18 states that the FSA will consider all the relevant circumstances of the case, which may include, but are not limited to, the factors set out at EG 9.9.

2.27 EG 9.19 states that the FSA will consider all the relevant circumstances when considering whether to grant or refuse an application to revoke or vary a prohibition order. EG 9.20 states that the FSA will take into account any indication given by the FSA in the final notice that it is minded to revoke or vary the prohibition order on application after a certain number of years.

2.28 EG 9.22 states that the FSA will not generally grant an application to revoke a prohibition order unless it is satisfied that it will not result in a reoccurrence of the risk to consumers or the financial system and the individual is fit to perform functions in relation to regulated activities.

Facts And Matters Relied On

2.29 Mr Redmond was at the relevant time a trader on the Freight Desk of Morgan Stanley's Commodities Division in London. He had held a position in Morgan Stanley's Commodities team for four years and had been promoted from Analyst to Associate during this period.

2.30 Mr Redmond was approved, under section 59 of the Act, to perform the CF30 'Customer' Controlled Function at Morgan Stanley. However, at the relevant time he carried out proprietary trading rather than trading for customer accounts.

2.31 Mr Redmond had worked on the Freight Desk since mid-2006 and his role involved both freight and oil trading. Mr Redmond had experience in trading oil products, including West Texas Intermediate Futures ("WTI Futures"). Mr Redmond understood that WTI Futures were highly liquid, vanilla instruments. Mr Redmond was responsible for submitting the daily P&L report for the Freight Desk.

2.32 On 6 February 2008, Mr Redmond took an extended lunch break between 13.14 and 16.41. He drank alcohol over lunch and it appears that this affected his behaviour on his return to the office, although he was not visibly drunk. Between 17.04 and 19.37 on 6 February 2008, Mr Redmond sold 24,868 lots and bought 19,493 lots of WTI Futures on the ICE web-based trading platform, WebICE. His trading represented over 30% of the total lots of WTI Futures traded on ICE on 6 February 2008. His short position reached 8,900 lots at 18.36. By 19.37, Mr Redmond had a substantial net short position of 5,395 lots.

2.33 At 20.04 on 6 February 2008, Mr Redmond transferred 5,400 lots of WTI Futures from his own strategy (account) to the strategy of one of his colleagues through a series of inter-strategy trades. Mr Redmond did this to try to conceal the substantial short position in WTI Futures. Mr Redmond's open short position of 5,395 lots was effectively neutralised with these inter-strategy trades. Mr Redmond's colleague had already submitted his own daily profit and loss figures and had left the office by this time. He did not know that Mr Redmond would be making the inter-strategy trades.

2.34 At 20.08, Mr Redmond submitted the P&L report into Morgan Stanley's risk management system. Given the inter-strategy trades he had made at 20.04, the effect of the P&L report did not reflect the substantial short position. Mr Redmond then transferred his substantial short position in WTI Futures back from his colleague's strategy to his own strategy by way of a further series of inter-strategy trades.

2.35 Traders in Morgan Stanley's Commodities Division were required to provide explanations to desk heads and senior management for large daily profit and loss movements. Whilst Mr Redmond initially increased his short position on 6 February when apparently trying to trade out of it, this is consistent with trying to avoid incurring a large profit or loss which would itself have drawn attention to Mr Redmond's trading. Mr Redmond was aware that, if he had committed his actual trading position to the firm's risk management systems, his short position would have breached the firm's VaR (value at risk) limits.

2.36 Mr Redmond left the office on 6 February 2008 without informing or attempting to inform his managers or any of his colleagues about the substantial short position he had created. Instead, by making the inter-strategy trades to his colleague's strategy before submitting the P&L report, Mr Redmond sought to conceal this position from Morgan Stanley. In the process, Mr Redmond breached Morgan Stanley's risk management systems and exposed the firm to the risk of incurring a significant loss. Mr Redmond accepts that this was a serious error of judgment on his part.

2.37 WTI Futures contracts are liquid and can be volatile instruments. The average market price in WTI Futures in the period 21 January 2008 to 22 February 2008 was $92.13. During that period, the price fluctuated by $14.40, between a high of $99.97 and a low of $85.57. On 6 February 2008, the price in WTI Futures fluctuated by more than $2, although in the two and a half hour period in which Mr Redmond traded, the price was relatively stable and Mr Redmond traded within a range of $0.78.

2.38 Using $2 as a benchmark (and the price could have moved outside this range), the substantial short position of 5,395 lots equates to an exposure to a possible loss of approximately $10 million. In the event, Mr Redmond traded out of his position on 7 February 2008 without making a substantial profit or loss.

2.39 On 7 February at 08.30, Mr Redmond cancelled all the inter-strategy trades he had made with his colleague’s strategy the night before.

2.40 On 7 February at 10.37, Mr Redmond started to buy back WTI Futures to reduce his substantial short position. By 13.56 on 7 February, he had closed the position and ceased trading. Mr Redmond still had not informed or attempted to inform his managers about the substantial short position or his attempt to trade out of that position, despite having had opportunities to do so.

2.41 Mr Redmond did not seek to offer any explanation to Morgan Stanley until he had discovered shortly after 14.00 on 7 February that Morgan Stanley was investigating his trading. Mr Redmond stated that he had made an error and ended up with a large short position overnight. He explained that he had decided to try to trade out of the short position before informing his managers. Mr Redmond did not admit to the inter-strategy trades to his colleague’s strategy until directly challenged about this. He accepts that he was trying to put the best possible light on his actions.

2.42 Mr Redmond was unable to provide a satisfactory explanation for his trading on 6 February. An analysis of Mr Redmond’s trading between 17.04 and 19.37 on 6 February shows that he traded almost continuously over this period, with an order on average every 7.5 seconds. The key strokes involved suggest that the orders were deliberate and were not caused by a manual error (such as leaning on the keyboard). Further, no technical errors were identified on Mr Redmond’s computer terminal.

2.43 Mr Redmond was suspended from Morgan Stanley on 7 February 2008 and was subsequently dismissed for gross misconduct on 10 March 2008 for (i) failing to properly escalate his short position in WTI Futures; (ii) attempting to conceal his short position from Morgan Stanley’s risk monitoring systems by transferring this to another strategy before submitting the P&L report; and (iii) exposing Morgan Stanley to significant potential exposure as a result of that open position.

2.44 Mr Redmond was employed by another firm between May and November 2008 when an application by that firm for approval of Mr Redmond was withdrawn. Mr Redmond has not been an approved person since 6 March 2008.

2.45 The FSA regards Mr Redmond's conduct on 6 and 7 February 2008 as demonstrating a serious lack of fitness and propriety. In particular, the FSA relies on the following matters:

- Mr Redmond submitted the P&L report on the evening on 6 February 2008 knowing that it did not reflect the true position, knowing that he was circumventing Morgan Stanley's risk management systems, and knowing that Morgan Stanley would, as a consequence, be unaware of the true risk to which it was exposed through the substantial short position he had created;
- Mr Redmond put Morgan Stanley at risk of incurring a significant loss by leaving the substantial short position unreported overnight on 6 February, in breach of the firm's procedures;
- Mr Redmond has been unable to provide a satisfactory explanation for his trading on 6 February or his failure to report this until after 14.00 on 7 February 2008;
- It appears that Mr Redmond panicked when he realised at some point after 17.04 on 6 February 2008 that he had a short position. Mr Redmond's instinctive reaction to hide his short position, to seek to trade out of it himself and not to report it or seek assistance shows a serious lack of judgment;
- Mr Redmond was under the influence of alcohol when he returned to the office on 6 February 2008 at 16.41;
- Mr Redmond missed a number of opportunities to report to his managers on 6 and 7 February 2008. For example, Mr Redmond had an opportunity to reflect overnight on 6 February and to make a full report to his managers on 7 February before he commenced trading out of the short position at 10.37 or finished doing so by 13.56; and
- Given his experience, Mr Redmond should have appreciated at the time that this was totally inappropriate conduct. The FSA finds that he showed a lack of honesty and integrity on 6 and 7 February 2008.

2.46 The FSA also notes that Mr Redmond was dismissed by Morgan Stanley for his conduct on 6 and 7 February 2008.

2.47 The FSA finds that Mr Redmond instinctively sought to conceal his substantial short position and his actions to trade out of that position on 6 and 7 February 2008, in particular by carrying out inter-strategy trades involving his colleague's strategy before submitting the P&L report. The guidance in FIT, in particular at FIT 1.3.1, FIT 2.10.1 and FIT 2.10.2, and the guidance in EG chapter 9, together suggest that it would be appropriate to make a prohibition order against Mr Redmond.

2.48 In the circumstances, the FSA finds that, as a result of his conduct on 6 and 7 February 2008, Mr Redmond is not a fit and proper person to perform functions in relation to a regulated activity carried on by any authorised person, exempt person or exempt professional person. Mr Redmond is not an approved person (although he was an approved person at the relevant time) so the appropriate sanction is prohibition rather than withdrawal of approval. The FSA makes an order prohibiting Mr Redmond from performing functions in relation to a regulated activity carried on by any authorised person, exempt person or exempt professional person.

2.49 In making a prohibition order in these terms, the FSA has taken into account all the relevant circumstances of the case including the circumstances in which Mr Redmond's conduct occurred. In addition to the matters summarised above, the FSA refers to the following matters:

- Mr Redmond's behaviour on 6 and 7 February 2008 appears to have been out of character. He had no record of previous misconduct, no previous concerns over his conduct or trading were identified and he had received good appraisals at Morgan Stanley;
- It appears that Mr Redmond was, to some extent, under the influence of alcohol when he commenced trading at 17.04 on 6 February 2008. It also appears that he felt under a degree of stress at work and that his judgment and recollection of events leading to the creation of the substantial short position by close of business on 6 February 2008 may have been impaired;
- The FSA notes that Mr Redmond's immediate managers were not in the office on the evening of 6 February 2008, although it appears that Mr Redmond did not attempt to contact them on 6 February and did not admit to the short position or the inter-strategy trades until after 14.00 on 7 February 2008;
- Mr Redmond's conduct took place over two days, in total a period of less than 24 hours, rather than over an extended period;
- It does not appear that Mr Redmond acted for his own personal benefit or financial gain or that his behaviour was premeditated;
- Given that he was carrying out proprietary trading, Mr Redmond's trading did not cause risk to consumers although it did put Morgan Stanley at risk;
- In the event, he was able to trade out of the substantial short position at a profit;
- Mr Redmond, who is now 28, has expressed remorse for his conduct, has admitted his actions and has taken responsibility for his actions; and
- Mr Redmond has co-operated with the FSA investigation and has agreed to settle this matter.

2.50 In the circumstances, whilst the FSA believes that a prohibition order is appropriate in order to achieve the FSA's regulatory objective of market confidence, the FSA would be minded to revoke the prohibition order after two years from the date of the Final Notice, upon application by Mr Redmond, in the absence of new evidence that Mr Redmond is not fit and proper.

3 DECISION MAKER

3.1 The decision which gave rise to the obligation to give this Final Notice was made by the Settlement Decision Makers on behalf of the FSA.

4 IMPORTANT

4.1 This Final Notice is given to Mr Redmond in accordance with section 390 of the Act

Publicity

4.2 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 Mr Redmond or prejudicial to the interests of consumers.

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

FSA contacts

4.4 For more information concerning this matter generally, you should contact Matthew Nunan (direct line: 020 7066 2672) of the Enforcement Division of the FSA.

Jamie Symington
Head of Department
FSA Enforcement Division