
FINAL NOTICE

To: **Winterflood Securities Limited**

Of: **The Atrium Building
Cannon Bridge
25 Dowgate Hill
London
EC4R 2GA**

Date: **22 April 2010**

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

THE ACTION

- 1 The FSA gave Winterflood Securities Ltd (“Winterflood”) a Decision Notice on 19 June 2008, imposing a financial penalty of £4 million on Winterflood for engaging in market abuse, pursuant to section 123 of the Financial Services and Markets Act 2000 (the “Act”). This penalty included an element of £900,000 representing disgorgement of estimated financial benefits arising from the market abuse.
- 2 The FSA decided to take action as a result of the behaviour of Winterflood for its part in the share ramping scheme which led to the suspension of trading in shares in Fundamental-E Investments Plc (“FEI”) by the Alternative Investment Market (“AIM”) on 15 July 2004. During the relevant period (5 January 2004 to 14 July 2004) Winterflood provided a market making service in the shares of FEI. Winterflood’s

conduct had the potential to, and did, cause serious loss to investors and damaged confidence in the AIM market.

- 3 Winterflood assisted in the share ramping scheme by:
 - 3.1 executing large numbers of rollovers thereby allowing payment for FEI shares to be avoided and thereby misleading the market;
 - 3.2 executing delayed rollovers thereby allowing payment for FEI shares to be avoided and thereby misleading the market;
- 4 As a direct result of its involvement in the scheme Winterflood caused:
 - 4.1 a false and misleading impression to be given to the market as to the demand for FEI shares; and
 - 4.2 a false and misleading impression to be given to the market as to the price or value of FEI shares.
- 5 On 17 July 2008 Winterflood referred the Decision Notice to the Financial Services and Markets Tribunal (“the Tribunal”). The substantive part of the Decision Notice is annexed to this Notice. On 22 January 2009 the Tribunal ordered, on the parties’ agreement, that two issues be tried as preliminary issues and that the hearing of the preliminary issues should be treated as the hearing of the Reference. Winterflood accepted the facts as they were stated in the FSA’s Statement of Case for the purpose of the determination of the Reference. The FSA’s Statement of Case can be found [here](#).
- 6 On 11 March 2009 the Tribunal considered the preliminary issues and in particular the effect of the Code of Market Conduct and whether an actuating purpose was needed to commit market abuse. The Tribunal determined that an actuating purpose was not necessary, dismissed Winterflood’s reference and ordered that the FSA should take the action referred to in its Decision Notice. The Tribunal’s written decision can be found on the Tribunal’s website [here](#).
- 7 Winterflood appealed and the hearing took place on 9 March 2010. The Court of Appeal dismissed Winterflood’s appeal and handed down its Judgment on 22 April 2010. A copy of the Judgment can be found [here](#).
- 8 Accordingly, the FSA hereby takes the action set out in the Decision Notice as directed by the Tribunal and imposes the financial penalty of £4 million.

IMPORTANT

- 9 This Final Notice is given in accordance with section 390 of the Act.

Manner of and time for payment

- 10 The financial penalty of £4 million must be paid in full by Winterflood by no later than 6 May 2010, 14 days from the date of the Final Notice.

If the financial penalty is not paid

- 11 If all or any of the financial penalty is outstanding on 6 May 2010, the FSA may recover the outstanding amount as a debt owed by Winterflood and due to the FSA.

Publicity

- 12 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 a 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 Winterflood or prejudicial to the interests of consumers.
- 13 The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA contacts

- 14 For more information concerning this matter generally, you should contact Karen Lee or Beth Harris at the FSA (direct line: 020 7066 1316 / 020 7066 2508).

Tracey McDermott
Head of Department
FSA Enforcement & Financial Crime Division

EXTRACT FROM DECISION NOTICE GIVEN BY THE FSA'S REGULATORY DECISIONS COMMITTEE TO WINTERFLOOD ON 19 JUNE 2008

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REASONS FOR THE ACTION

Introduction

1. The FSA has decided to take this action as a result of the behaviour of Winterflood during the period 5 January 2004 to 14 July 2004, inclusive, (the "relevant period") for its part in the share ramping scheme which led to the suspension of trading in shares in Fundamental-E Investments Plc ("FEI") by the Alternative Investment Market ("AIM") of the London Stock Exchange (the "LSE") on 15 July 2004. Shares in FEI were suspended on 15 July 2004 for a week and on further trading the share price fell dramatically and has never recovered. Winterflood's conduct had the potential to, and did, cause serious loss to investors and damaged confidence in the AIM market.
2. Winterflood is a London based market maker in over 2,600 UK equities and provides a trading service in North American and European markets. Winterflood has positioned itself as a specialist in AIM and smaller company securities. During the relevant period Winterflood provided a market making service in the shares of FEI and was authorised and continues to be authorised.
3. Simon Eagle ("Mr Eagle"), the controller of SP Bell Ltd ("SP Bell") and a director of FEI, embarked on a deliberate course of market abuse in relation to FEI through the use of rollovers, delayed rollovers and the manipulation of share prices.
4. Mr Eagle required the participation of Winterflood in order to implement his scheme. He relied on Winterflood's assistance to:
 - 4.1 execute large numbers of rollovers and thereby avoid paying for FEI shares and thereby mislead the market;
 - 4.2 execute delayed rollovers and thereby avoid paying for FEI shares and thereby mislead the market;
 - 4.3 position the share price of FEI at an artificially high level.
5. As a direct result of its involvement in the scheme Winterflood caused:
 - 5.1 a false and misleading impression to be given to the market as to the demand for FEI shares; and
 - 5.2 a false and misleading impression to be given to the market as to the price or value of FEI shares.

6. It appears to the FSA, on the basis of the facts and matters described below, that Winterflood's behaviour amounted to market abuse contrary to s118 (2)(b) and 118 (2)(c) of the Act (as in force at the relevant period) as follows:
 - 6.1 it occurred in relation to a qualifying investment traded on a prescribed market (i.e. FEI shares traded on AIM);
 - 6.2 it was:
 - 6.2.1 likely to give a regular user of the market a false or misleading impression as to the supply of, demand for, price or value of, FEI shares; and
 - 6.2.2 such that a regular user of the market would, or would be likely to, regard the behaviour as that which would, or would be likely to, distort the market in FEI shares;
 - 6.3 it is likely to be regarded by a regular user of that market who is aware of the behaviour as a failure on the part of Winterflood to observe the standard of behaviour reasonably expected of a person in Winterflood's position in relation to the market; and
 - 6.4 it occurred in the United Kingdom.

Market abuse: Relevant Statutory Provisions

7. Section 118 of the Act defines market abuse. References in this Notice to provisions of this part of the Act are to those in force during the period of the behaviour referred to. In particular, section 118(1) of the Act provides as follows:

“For the purposes of this Act, market abuse is behaviour (whether by one person alone or by two or more persons jointly in concert):

- (a) which occurs in relation to qualifying investments traded on a market to which this section applies;*
- (b) which satisfies any one or more of the conditions set out in subsection (2); and*
- (c) which is likely to be regarded by a regular user of that market who is aware of the behaviour as a failure on the part of the person or persons concerned to observe the standard of behaviour reasonably expected of a person in his or their position in relation to the market.”*

8. Section 118(2) of the Act provides (so far as relevant to this Notice) as follows:

“The conditions are that -

- (a) ...*

- (b) *the behaviour is likely to give a regular user of the market a false or misleading impression as to the supply of, or demand for, or as to the price or value of, investments of the kind in question;*
 - (c) *a regular user of the market would, or would be likely to, regard the behaviour as behaviour which would, or would be likely to, distort the market in investments of the kind in question.”*
9. Under The Financial Services and Markets Act 2000 (Prescribed Markets and Qualifying Investments) Order 2001 (made under section 118(3) of the Act):
- 9.1 all markets operated under the rules of a UK recognised investment exchange (which includes the AIM market operated by the London Stock Exchange) are prescribed markets; and
 - 9.2 all investments specified for the purposes of defining a regulated activity (including shares traded on AIM) are qualifying investments.

The Code of Market Conduct

10. Section 119 of the Act provides as follows:
- “(1) *The Authority must prepare and issue a code containing such provisions as the Authority considers will give appropriate guidance to those determining whether or not behaviour amounts to market abuse.*
 - (2) *The code may among other things specify-*
 - (a) *descriptions of behaviour that, in the opinion of the Authority, amount to market abuse;*
 - (b) *descriptions of behaviour that, in the opinion of the Authority, do not amount to market abuse;*
 - (c) *factors that, in the opinion of the Authority, are to be taken into account in determining whether or not behaviour amounts to market abuse.*
 - (3) *The code may make different provision in relation to persons, cases or circumstances of different descriptions. ...”*
11. The FSA has issued the Code of Market Conduct (“The Code”) under section 119 and it forms the first section of the Market Conduct Sourcebook (MAR 1) in the FSA’s Handbook of rules and guidance. References in this Notice to provisions of The Code (or MAR 1) are to the provisions in force at the time of the behaviour described in this Notice.
12. Section 122 of the Act provides as follows:

- “(1) *If a person behaves in a way which is described (in the code in force under section 119 at the time of the behaviour) as behaviour that, in the Authority’s opinion, does not amount to market abuse that behaviour of his is to be taken, for the purposes of this Act, as not amounting to market abuse.*
- (2) *Otherwise, the code in force under section 119 at the time when particular behaviour occurs may be relied on so far as it indicates whether or not that behaviour should be taken to amount to market abuse.”*
13. In accordance with section 122(2) of the Act, provisions of the Code identified by the letter ‘E’ may be relied upon so far as they describe behaviour which, in the opinion of the FSA, amounts to market abuse or in accordance with section 119(2)(c) of the Act, describe factors that, in the opinion of the FSA, are to be taken into account in determining whether or not behaviour amounts to market abuse. (MAR 1.1.11G)
14. The Code is not an exhaustive list of the types of behaviour that may or may not be market abuse, nor does it contain an exhaustive list of the factors to be taken into account in determining whether behaviour is or is not market abuse. (MAR 1.1.13G)

False or misleading impression (section 118(2)(b))

15. Behaviour which is likely to give a regular user of the market a false or misleading impression as to the supply of, demand for or price or value of the investments in question is market abuse (section 118(2)(b) of the Act). The relevant parts of the Code are contained in MAR 1.5. In particular, MAR 1.5.3E provides that:
- “Prescribed markets provide a mechanism by which the price or value of investments may be determined according to the market forces of supply and demand. When market users trade on prescribed markets they expect the price or value of investments and volumes of trading to reflect the proper operation of market forces rather than the outcome of improper conduct by other market users. Improper conduct which gives market users a false or misleading impression results in market users no longer being able to rely on the prices formed in markets or volumes of trading as a basis for their investment decisions. This will undermine confidence in the integrity of the prescribed market and overall market activity may decrease and transaction costs may rise, or both, to the detriment of market users, including investors.”*
16. The Code gives a number of examples of behaviour amounting to market abuse of this type, including artificial transactions. MAR 1.5.8E notes the characteristics of one type of artificial transaction that does, in its opinion, amount to market abuse, as follows:
- (a) the principal effect of the transaction is to, inter alia, inflate or maintain the apparent demand for or the apparent price or value of the share;
- (b) the person concerned knows or can reasonably be expected to know this principal effect;

except when the principal rationale is a legitimate commercial rationale and the transaction is executed in a proper way.

17. A transaction which creates a false or misleading impression will not normally be considered to have a legitimate commercial rationale where the purpose behind the transaction was to induce others to trade in or to position or move the price of a security (MAR 1.5.9E).
18. A transaction will be executed in a proper way where it is executed in a way which takes into account the need for the market as a whole to operate fairly and efficiently (MAR 1.5.10E).
19. Factors that are to be taken into account in determining whether or not behaviour amounts to market abuse, including the following (MAR 1.5.11E):
 - (a) whether the transaction causes or contributes to an increase in the demand for or the price or value of a security and the person responsible for the transaction has an interest in the level of demand for or the price or value of the security;
 - (b) whether the transaction involves the placing of buy and sell orders at prices higher or lower than the market price or the placing of buy and sell orders which increase the volume of trading.
20. A person has an interest in a security where he may directly or indirectly benefit from alterations in its market price (MAR 1.5.13E).

Distortion (section 118(2)(c))

21. Behaviour which would, or would be likely to, distort the market in the investment in question is market abuse (section 118(2)(c) of the Act). The Code deals with distortion at MAR 1.6. In particular, MAR 1.6.3E states:

“...A person may not engage in behaviour that interferes with the proper operation of market forces and so with the interplay of proper supply and demand and so has a distorting effect. Distortion undermines confidence in the prescribed markets and damages efficiency to the detriment of market users, including investors.”
22. MAR 1.6.4E sets out the FSA’s opinion that behaviour will amount to market abuse if it interferes with the proper operation of market forces with the purpose of positioning prices at a distorted level.
23. MAR 1.6.7E notes that behaviour which falls within the descriptions of distortion in the Code may also fall within the scope of the prohibition of behaviour giving rise to a false or misleading impression.
24. The Code gives examples of behaviour amounting to distortion, including price positioning. MAR 1.6.9E states that behaviour will constitute market abuse where a

person enters into a transaction, or a series of transactions, with the purpose of positioning the price of a security at a distorted level.

25. Factors to be taken into account in determining whether behaviour amounts to market abuse, include the following (MAR 1.6.11E):
- (a) the extent to which the person concerned had a direct or indirect interest in the price or value of the security;
 - (b) the volume or size of the person's transaction or transactions in relation to reasonable expectations as the depth and liquidity of the market at the time in question;
 - (c) whether a person has successfully and consistently increased the prices he had paid for a security.

Facts and Matters Relied On In the Warning Notice

(a) SP Bell

26. SP Bell was an agency only stock broking firm which conducted business from nine branch offices located throughout the UK, including Manchester. SP Bell was authorised by the FSA to conduct investment business, and was a member of the LSE. On 27 May 2003 Mr Eagle acquired SP Bell using an investment vehicle. At all times thereafter Mr Eagle owned and controlled SP Bell.

(b) The initial FEI transaction

Mr Eagle's activities

27. Mr Eagle had been actively seeking to secure control of an AIM shell company as an investment vehicle to acquire electronic technology companies and in May 2003 he agreed with the two majority shareholders of FEI (the "original shareholders") that he would arrange for their shares, 85% of the issued share capital (140 million shares), to be sold.
28. Mr Eagle proposed to buy a 10% stake in FEI himself: however, he had to find buyers for the remaining 75%. He proposed to do so, for the most part, by selling shares to clients of SP Bell.
29. There was little or no current market demand for FEI shares (it was a company specialising in electronic components but was increasingly out of step with current technology). During May 2003 a total of 109,019 shares were traded. Therefore Mr Eagle had to generate significant demand in order to achieve the share sale.
30. Mr Eagle and Mr Betton (another director and broker of SP Bell) orchestrated a sales campaign from August 2003 whereby SP Bell brokers arranged the sale of 35.9 million FEI shares to SP Bell clients. Mr Eagle himself took 16.5 million shares (through an investment vehicle) and marketed FEI shares to other brokers, whose clients purchased 20.3 million shares. Mr Betton caused 30 of his clients to take up 16.1 million shares between 13 August 2003 and 5 December 2003 and strongly encouraged other brokers to recommend FEI shares to their clients. In addition, Winterflood sold some shares as part of its normal market making business. However, there remained a significant rump of shares for which no purchasers had been found.
31. In order to procure purchasers for the outstanding rump of FEI shares, Mr Eagle himself introduced 50 new clients to SP Bell during the period 18 July 2003 to 13 May 2004. 27 of these clients bought 60.7 million FEI shares, thus completing the sale of shares by the end of December 2003 and giving Mr Eagle control of FEI.
32. Between 13 August and 31 December 2003 SP Bell purchased 113,045,675 FEI shares from Winterflood, ostensibly on behalf of its clients.

33. On 19 November 2003 Mr Eagle became a director of FEI. On 5 January 2004 he became executive chairman of FEI. He was actively involved in the management of the company.

Winterflood's involvement

34. In July 2003 Mr Eagle met two market makers employed by Winterflood, including Stephen Sotiriou who was responsible within Winterflood for making a market in FEI shares. Mr Eagle informed them that he intended to take over FEI, that the owners of 85% of the shares would approach Winterflood to sell their shares, and that Mr Eagle would then buy the stock from Winterflood. The market makers were surprised at this method being used rather than SP Bell carrying out internal agency crosses. Even so, Mr Eagle did use Winterflood to intermediate the sale of the FEI shares. The original shareholders sold their shares, via third party brokers, to Winterflood. Winterflood sold them in turn to purchasers sourced by Mr Eagle and SP Bell.
35. Winterflood's intermediation of the sale of these shares allowed Mr Eagle to obscure the full extent of his financial interest and involvement in the FEI share sale from the employees of SP Bell, the clients of SP Bell to whom a purchase of shares was recommended and from the market generally. In particular, it allowed Mr Eagle to conceal the fact that he stood to earn a significant commission from the vendors.
36. Winterflood's intermediation of the sale of these shares was highly remunerative. It received a total financial benefit from these transactions of £204,403 on proceeds of £3,053,155. Winterflood's participation was largely risk-free.
37. As market maker in FEI shares, Winterflood knew that there had been little or no active market before Mr Eagle's proposal to arrange the sale of FEI shares by the original shareholders. In addition, Winterflood knew that:
- 37.1 as owner of SP Bell and an intended director of FEI, Mr Eagle was acting on both sides of the sale by the original owners of their shares;
 - 37.2 there was no reason why this stock could not be crossed internally at SP Bell rather than being put through the market-maker, which process involved a cost to the underlying clients taking up the shares with no compensating benefit;
 - 37.3 routing this trading through a market-maker was not the normal way of conducting this sort of business;
 - 37.4 trading via Winterflood would result in the dealings being reported to the market as ordinary trades rather than as agency crosses;
 - 37.5 Mr Eagle himself proposed to take, and did take (on 11 November 2003 via an investment vehicle) a 10% stake in FEI.
38. These circumstances were highly unusual. Winterflood recognised this, and accordingly, if it had observed the standards reasonably expected of a market maker, at the very least, Winterflood should have been alerted and should have questioned the pattern of subsequent trading by SP Bell in FEI shares. Winterflood did not do so.

(c) **The rollover scheme**

39. In order to avoid certain SP Bell clients being required to pay for their FEI shares, Mr Eagle instituted a scheme whereby FEI positions were rolled from one SP Bell client account to another. The effect of the rollover trades was to defer settlement, potentially indefinitely. The method used was for SP Bell:
- (a) to buy FEI shares for a client on a “T+10” settlement basis (in effect the client buys on credit by settling the trade ten days after the trade date); and
 - (b) to sell those shares (via the market maker) to another client at or before the date of settlement (typically SP Bell sold shares on a “T + 2” basis).

A rise in share price which had occurred in the intervening period covered the cost of purchase and left a profit on the first account which could then be used to purchase further FEI shares. The rollover scheme thus required a rising share price in order to succeed in deferring settlement.

40. The rollover scheme not only allowed Mr Eagle to complete the sale of the 140 million shares by the two majority shareholders, it also allowed him to continue to buy shares in the market as required in order to position the price of FEI shares at an artificial level, as set out in more detail below. Between January and July 2004, SP Bell bought 42,115,450 shares in the market. It bought 25,703,550 of those shares from Winterflood. These shares were not paid for but were simply added into the rollover scheme.
41. Winterflood executed rollover trades for SP Bell from 24 September 2003 to 31 December 2003:
- 41.1 in September 2003, SP Bell rolled over 4,572,000 FEI shares in two rollover trades (total volume 9,144,000 FEI shares);
 - 41.2 in October 2003, SP Bell rolled over 1,788,000 FEI shares in one rollover trade (total volume 3,576,000 FEI shares);
 - 41.3 in November 2003, SP Bell rolled over 11,370,000 FEI shares in 13 rollover trades (total volume 22,740,000 FEI shares); and
 - 41.4 in December 2003, SP Bell rolled over 17,262,000 FEI shares in 14 rollover trades (total volume 34,524,000 FEI shares).
42. As a result of these trades, Winterflood knew that a number of SP Bell clients had rolled their positions in FEI from September 2003. The FSA does not allege that Winterflood knew Mr Eagle’s purpose in starting the rollover scheme. The FSA also accepts that it was reasonable for Winterflood to assume that the rollovers during the period 24 September to 31 December 2003 were proper and genuine.
43. SP Bell continued to buy shares from, and roll shares with, Winterflood in the period January to July 2004. The vast majority of the rollover trades were executed by Winterflood. The volume of FEI shares that were rolled over by Winterflood

amounted to around 84% of the volume of FEI share trades reported by all firms in this period. Between January and July 2004 the volume of FEI shares that were rolled over by Winterflood totalled 1.6 billion shares. Details are given below:

Month	Number of shares bought	Number of shares rolled (number of trades)
January	3,015,000	68,059,000 (24)
February	4,655,000	81,809,000 (36)
March	2,688,300	87,300,000 (21)
April	785,000	130,684,000 (34)
May	4,360,250	130,365,000 (21)
June	8,700,000	235,851,018 (90)
1-14 July	1,300,000	87,599,786 (32)

44. Rule 3050 of the LSE Rules provides that a member firm may carry out a rollover trade in respect of any position in a relevant security on one occasion only. For this purpose a “rollover trade” is defined as a set of on-exchange transactions, the effect of which is to postpone the final settlement of a position in a security by closing an existing unsettled transaction and entering into a transaction in the same security which creates a new position for settlement at a later date. The purpose of the rule is to ensure that all trades are settled promptly, thus protecting the proper operation and integrity of the market.
45. SP Bell breached LSE Rule 3050 in that individual positions were rolled over more than once (on the instructions of Mr Eagle). However, the FSA accepts that it was reasonable for Winterflood to assume that the rollovers carried out between 24 September and 31 December 2003 were in compliance with LSE Rule 3050.
46. However, any rollovers associated with the initial disposal of the shares would have ended once the T+10 settlement period for trades executed on 30 December 2003 had elapsed. Thus, by 28 January 2004, it would not be reasonable to assume that any further rollovers were associated with the initial purchase of the shares.
47. These trades were consistently undertaken with a mismatch in settlement dates: shares were predominantly sold on a T+2 basis and bought on a T+10 basis. Such a consistent trading pattern is a clear indicator that the trades are rollovers within the terms of LSE Rule 3050.
48. The volume of shares being rolled over dwarfs the number of FEI shares being bought throughout this period. Rollovers of this volume and frequency are highly unusual. Winterflood knew that the volume of rollovers was massive and dominated the market in FEI shares.
49. The rollover trades took place in the context of the following matters each of which was known to Winterflood:
 - 49.1 the unusual circumstances surrounding the initial sale of 140 million shares by the original shareholders;

- 49.2 27 delayed rollover trades executed by Winterflood for SP Bell between January and March 2004;
 - 49.3 an apparently limitless appetite by SP Bell customers for FEI shares offered to the market, regardless of market conditions; and
 - 49.4 a series of requests from Mr Eagle/SP Bell to Winterflood to increase the FEI share price.
50. In these circumstances, a market maker acting in accordance with the standards reasonably expected of him should have concluded that:
- 50.1 these trades were rollover trades within the terms of LSE Rule 3050 rather than put-through trades; and
 - 50.2 there was, at the least, a clear and substantial risk that the rollovers executed on or after 28 January 2004 were not proper and genuine trades.
51. Having been alerted to the risks associated with this pattern of trading, a market maker acting in accordance with the standards reasonably expected of him should have asked questions of SP Bell in order to satisfy itself that the trades were proper and genuine and should have discontinued executing such trades if it was not so satisfied.
52. At no stage did Winterflood question SP Bell about the purpose of the rollover trades. Another market maker did question SP Bell about the purpose of the rollover trades conducted with it, in the context of a much lower volume of rollovers (just under 80 million shares). SP Bell assured that market maker that the rollovers were genuine and for different customers.
53. The rollover trades were not genuine trades but were reported to the market as ordinary trades. As such they concealed from the market that a significant amount of FEI shares had not been paid for and gave a false and misleading impression as to the level of demand for FEI shares. The rollover trades were an essential element of the share ramping scheme.
54. By executing the rollover trades, SP Bell, with the participation of Winterflood, deliberately deferred settlement of the trades and deliberately concealed from the market that a significant amount of FEI shares had not been paid for. Had this been known to the market, it is highly likely that it would have caused a significant fall in the FEI share price.
55. By executing the rollover trades Winterflood caused the market to be given the impression that there was substantial and continuous demand for FEI shares. This was not in fact the case.
56. Winterflood took a turn on each rollover trade and received financial benefits of £777,652.

(d) Constant source of buyers

57. As noted above, between January and July 2004, SP Bell bought 42,115,450 shares in the market. It bought 25,703,550 of those shares from Winterflood. This trading did not represent genuine market demand for the shares. It was artificial. In many cases it was unauthorised by the underlying clients. These trades were undertaken by SP Bell in the knowledge that there was no means of paying for them. These shares were not paid for but were simply added into the rollover scheme. SP Bell bought these shares in order to facilitate the positioning of the price at an artificial level.
58. Winterflood knew that the trading by SP Bell clients was highly unusual:
- 58.1 If there was FEI stock available, whether being offered to the market or a long position accumulated by Winterflood which it wished to sell down, SP Bell could generally be relied upon to buy stock. This was the case in most circumstances, regardless of the current share price, any negative market information or a preponderance of sellers. This consistent buying interest from clients of a single broker at increasing prices regardless of market conditions is highly unusual.
- 58.2 Private clients are typically independently minded and deal at a time which suits them or when prompted by developments in a stock. Clients making their own dealing decisions can be expected to react to market movement, comment or announcements. Yet on days where FEI stock had been tipped in the press (e.g. 5 January 2004, 5 April 2004, 10 May 2004 and 31 May 2004) or where there had been significant moves in the share price (e.g. 5 May 2004) there was very little, if any, trading by SP Bell clients.
- 58.3 SP Bell did not take time to obtain instructions from its clients prior to trading when approached by Winterflood to buy stock nor when they were asked to make significant changes to the scope of an order.
59. Further Winterflood knew that Mr Eagle was in a position of a conflict of interest in that Winterflood knew that:
- 59.1 Mr Eagle was a director of and substantial shareholder in FEI and as such had an interest in increasing the FEI share price;
- 59.2 Mr Eagle was the controller of SP Bell and was obliged to act in the best interests of SP Bell clients.
60. In these circumstances, a market maker acting in accordance with the standards reasonably expected of him would have concluded, at the least, that there was a clear and substantial risk that the trading on behalf of SP Bell clients was not proper or genuine.
61. Having been so alerted, a market maker acting in accordance with the standards reasonably expected of him should have asked questions of SP Bell in order to satisfy itself that the trades were proper and genuine and should have discontinued executing

such trades if it was not so satisfied. Winterflood did not question the purpose of this trading and continued to trade in essentially the same way with SP Bell until July 2004.

(e) Delayed rollovers

62. Between 5 January and 18 March 2004 Winterflood executed 27 delayed rollovers for SP Bell (acting at the instigation of Mr Eagle), whereby the two legs of the transaction were executed at different times of the day, although the size and price of the second leg of the transaction were agreed at the outset.
63. Such delayed rollovers are highly unusual. Further, they are highly misleading to the market. The time lapse between the execution of the two legs of the trade makes it impossible for market participants to identify the trades as rollovers. Such trades will appear to be genuine and unrelated trades driven by the economic forces of supply and demand.
64. The delayed rollovers involved high volumes of shares: 190.5 million in total, more than the entire issued share capital of the company. Such high volume trading, which represented 40.5% of the market within this short period of time, gave a significantly misleading impression to the market.
65. In addition the delayed rollovers were often transacted at the top end of the touch price, thus giving the impression to market participants that there was sustained buying interest at higher prices.
66. The delayed rollovers were not proper and genuine trades. In many cases they were not authorised by the underlying customers. They were an essential element of the share ramping scheme.
67. The delayed rollover trades took place in the context of the following matters, each of which was known to Winterflood:
 - 67.1 the unusual circumstances surrounding the initial sale of 140 million shares by the original shareholders;
 - 67.2 the massive and increasing volume of rollover trades executed by Winterflood for SP Bell between January and July 2004;
 - 67.3 an apparently limitless appetite by SP Bell customers for FEI shares offered to the market, regardless of market conditions; and
 - 67.4 a series of requests from Mr Eagle/SP Bell to Winterflood to increase the FEI share price.
68. In these circumstances, a market maker, acting in accordance with the standards reasonably expected of him, would have concluded, at the least, that there was a clear and substantial risk that the 27 delayed rollovers executed between 5 January and 18 March 2004 were not genuine or proper trades. Therefore Winterflood, if acting in accordance with the standards reasonably expected of a market maker, should have

asked questions of SP Bell in order to satisfy itself that the trades were proper and genuine and should have discontinued executing such trades if it was not so satisfied.

69. Winterflood did not ask any questions of SP Bell about any of the delayed rollovers and continued to execute such trades for SP Bell until 18 March 2004. On or shortly before that date, and as a result of concerns as to the propriety of the trades, Winterflood decided not to execute further delayed rollovers.
70. By executing the delayed rollovers Winterflood caused the market to be given the false and misleading impression that there was substantial and continuous demand for FEI shares. This conduct fails to meet the standards reasonably expected of a market maker.

(f) Involvement of Winterflood Directors

71. Two of the directors responsible for trading matters reviewed trading in FEI on most days from February 2004. The directors knew of:
 - 71.1 the volume of rollover trades;
 - 71.2 the volume of purchases by SP Bell;
 - 71.3 the volume of non-SP Bell trading; and
 - 71.4 the increases in the share price.
72. In these circumstances, the directors of a market maker, acting in accordance with the standards reasonably expected of them, would conclude that there was a clear and substantial risk that the apparently unlimited demand for FEI shares from clients of SP Bell was not genuine and that trades being executed by Winterflood with SP Bell's clients were not proper or genuine trades, and that as a consequence there was no proper basis for increases in the bid/offer quote.
73. Furthermore, having been so alerted, the directors of a market maker, acting in accordance with the standards reasonably expected of them, would have required the traders responsible for the relationship with SP Bell to ask questions of SP Bell as to the nature of the trades, in order to satisfy themselves that the trades were proper and genuine and to discontinue the trades if they were not so satisfied. Contrary to this, when, in May 2004 a Winterflood trader escalated concerns regarding the trading in FEI to the directors, he was instructed by the directors to continue trading.
74. The directors failed to address, adequately or at all, any of the following:
 - 74.1 the clear and substantial risk that the apparently unlimited demand for FEI shares from clients of SP Bell was not genuine;
 - 74.2 the clear and substantial risk that the rollover trades and the delayed rollovers were not proper or genuine; and

- 74.3 the clear and substantial risk that there was no proper basis for the increases in the bid/offer quote.
75. The FSA considers the directors' instruction to the trader to continue trading, despite his having raised legitimate concerns, to be a serious failure to act in accordance with the standards reasonably expected of the directors of a market maker.
- (g) Manipulation of the share price**
76. By January 2004, in order for the rollover scheme to continue (i.e. to avoid the Eagle Accounts needing to fund purchases of FEI shares), Mr Eagle needed continued increases in the share price of FEI.
77. Mr Eagle also needed to achieve an increase in the share price for the following reasons:
- 77.1 to generate "profits" on the rollover accounts which could be used to fund further purchases of shares, thereby helping to ensure that any selling into the market would not depress the price;
- 77.2 to enable FEI to fund acquisitions of other companies using stock as consideration;
- 77.3 to enable FEI to raise capital in the market to fund further acquisitions; and
- 77.4 to attract genuine retail and institutional investors to FEI.
78. Accordingly, in January 2004 Mr Eagle embarked on a deliberate programme of share price manipulation whereby he sought to position the price of FEI shares at an artificially high level. Mr Eagle's aims were:
- 78.1 to attract media and investor attention to FEI through a combination of price rises and increased volume; and
- 78.2 to secure an increasing share price in order that the rollover scheme might continue, that corporate acquisitions be funded, and that retail and institutional investors be attracted to the stock.
79. There are, broadly speaking, three phases of the share price manipulation scheme that can be identified:
- 79.1 during January to March 2004:
- FEI undertook two corporate acquisitions, the consideration for which was shares in FEI;
 - Winterflood raised its bid/offer quote 12 times;

- Winterflood executed 54 rollovers (not including delayed rollovers) with a total volume of 285.4 million shares and 27 delayed rollovers with a total volume of 190.4 million shares for SP Bell; and
- an article in the Daily Mail on 13 January 2004 reported that a “hefty” 11.7 million shares had been traded and that FEI could be one to watch;

79.2 during April 2004:

- the share price manipulation scheme was beginning to have the desired effect:
 - there were a number of favourable articles in the press; and
 - the level of investor interest was growing;
- Winterflood raised its bid/offer quote 13 times; and
- Winterflood executed 34 rollovers with a total volume of 261.3 million shares for SP Bell; and

79.3 during May to July 2004:

- the level of media and investor interest in FEI had tailed off - it was more difficult to attract media and investor attention to FEI and to secure an increasing share price because of the lack of investor interest in the stock at the higher prices then prevailing;
- the volumes of trading were significantly lower;
- FEI undertook a share placing to raise £2,520,000 and two corporate acquisitions during this period; the consideration for one acquisition was shares in FEI;
- Winterflood raised its bid/offer quote 10 times; and
- Winterflood executed 149 rollovers with a total volume of 908 million shares for SP Bell.

80. There was an unusually close relationship between Mr Eagle and Winterflood. This is demonstrated by the following:

80.1 a high degree of information sharing – in particular Winterflood traders freely discussed their book positions with Mr Eagle and SP Bell;

80.2 SP Bell brokers were instructed by Mr Eagle to deal only with Winterflood when trading FEI shares; and

- 80.3 obvious pre-arranging of trades – there were frequent instances where Winterflood traders spoke first to Mr Eagle on an untaped line and then conducted the trade with SP Bell on a taped line.
81. Furthermore, there was an unusually high level of communication between Mr Eagle and Winterflood on untaped lines during the period 1 January 2004 to July 2004 as demonstrated by the numerous conversations on mobile telephones between Winterflood employees and Mr Eagle. In particular the Winterflood market maker Mr Sotiriou made 41 calls on his mobile to Mr Eagle and sent one text; and Mr Eagle made 71 calls to Mr Sotiriou's mobile. Mr Sotiriou's mobile telephone records do not show a similar level of communication with other brokers. The FSA has concluded that at least some of the calls were undertaken on mobile telephones in order to avoid those conversations being taped.
82. Winterflood demonstrated co-operation in the share price manipulation scheme as follows:
- 82.1 the willing execution of rollover and delayed rollover trades (described above);
- 82.2 the decision by senior management to continue rollover trades despite internal concerns having been raised (described above); and
- 82.3 consistent co-operation in increasing its bid/offer quotes including in response to requests instigated by Mr Eagle (described below).
83. Winterflood from time to time failed to use its independent judgment as to the appropriate pricing for FEI stock (which is the standard reasonably to be expected of a market maker), including by consistently acceding to requests instigated by Mr Eagle to increase its bid/offer quote.
- 83.1 Between 2 January 2004 and 14 July 2004 the share price of FEI increased from 4.13p to a high of 11.75p. There were 43 upward moves in the quote to establish a new offer price during this period. The share price continued to rise even when demand for the shares (other than that attributable to Mr Eagle's instructions) was falling.
- 83.2 Of these upward movements, 35 were led by Winterflood, which was at all times the dominant market maker in FEI shares. On at least 15 occasions the increases are not obviously referable to the level of genuine supply and demand, by reference to orders placed by SP Bell, nor referable to anticipated further demand by SP Bell.
- 83.3 SP Bell, at the instigation of Mr Eagle, specifically requested Winterflood to increase the bid/offer quote. Winterflood consistently co-operated with these requests, none of which are obviously referable to the trading and market conditions prior to the quote increase. For example:

- On 5 January 2004 SP Bell asked Winterflood to increase its quote at 13:23 and Winterflood increased its quote at 13:24 from 4.00p/5.00p to 4.25p/5.25p. There were a number of untaped calls between Mr Eagle and Winterflood traders prior to the quote move. Most trading activity had taken place in the morning, the largest of which was a buy trade by Winterflood at the bid side leaving Winterflood with a long position. This was the first leg of a delayed rollover. It was apparent that the delayed rollover would result in SP Bell buying back the shares (with a small adjustment) later that day;
- On 2 February 2004 Winterflood increased its quote at 15:13 from 4.75p/5.75p to 5.00p/6.00p. There were a number of untaped calls between Mr Eagle and Winterflood traders prior to the quote move. The FSA infers from this that Mr Eagle requested an increase in the quote. Trading with market participants prior to the increase was on the bid/mid side of the market and left Winterflood with a long position. After the quote increase, another market maker challenged the increase by offering shares at the new bid price. A buy-side firm then sought to transact business at the bid side but Winterflood refused to complete their total size;
- On 2 March 2004 SP Bell asked Winterflood to increase the quote at 12:24 and Winterflood increased its quote at 12:27 from 5.00p/6.00p to 5.25p/6.25p. Trading was light, with only a sale on the bid side which maintained Winterflood's long position; and
- On 15 March 2004 Winterflood increased its quote at 11:00 from 6.00p/7.00p to 6.25p/7.25p. There were a number of untaped calls between Mr Eagle and Winterflood traders prior to the quote increase. In a conversation at 11:03 Winterflood advised SP Bell that it had increased its quote as it understood that SP Bell/Mr Eagle wished to see an improvement in the share price. The FSA infers from this that Mr Eagle requested an increase in the quote. FEI had issued a negative announcement that morning of a significant fall in pre-tax profits and a dividend cut.

84. Winterflood's increases to its bid/offer quote including at the instigation of Mr Eagle caused the price of FEI shares to be positioned at an artificially high level. This had the effect of misleading the market as to the price or value of FEI shares and of distorting the market in FEI shares. The market was also misled by the apparent volume of trading, share price and trading pattern.
85. The quote increases and the trading at the higher share prices gave the market a false and misleading impression as to the price or value of FEI shares and caused the price to be positioned at an artificially high level. Such price positioning at an artificial level also amounts to market distortion.
86. Winterflood received benefits from SP Bell, which it did not question, in the form of:

- 86.1 unusually high remuneration on transactions;
- 86.2 a supply of buyers for Winterflood's long positions; and
- 86.3 occasional assistance from SP Bell in minimising Winterflood's overnight exposure to long positions in FEI, for example the adjustment by SP Bell (without having or seeking any instructions from its clients) of the size of a transaction during a conversation between Mr Sotiriou and Mr Betton on 2 February 2004 in order to allow Winterflood to flatten its book in FEI shares.
87. The unusually close relationship, the significant and unusual amount of communication on untaped lines, the uncritical co-operative actions and the benefits received by Winterflood, all taken together, created a pattern of behaviour which had the effect of Winterflood allowing Mr Eagle (directly or through SP Bell) from time to time during the period January 2004 to July 2004 to control Winterflood's pricing of FEI shares.
88. Accordingly, with the co-operation of Winterflood, Mr Eagle achieved a series of increases in the bid/offer quote which had the effect of positioning the price of FEI at an artificially high level.
89. Winterflood's overall behaviour amounted to a failure to act in accordance with the standards reasonably expected of a market maker. In particular Winterflood, in the context of its unusually close relationship with SP Bell, the significant amount of communication on untaped lines and the pattern and volume of co-operative trading between the two in FEI shares, should have been alert to the consistently increasing price quotations for FEI resulting from that combination and should have ceased to co-operate unquestioningly with SP Bell. Winterflood failed to review its relationship with SP Bell and continued to co-operate in the share price manipulation scheme.
- (h) Other matters**
90. The trading in FEI was profitable for Winterflood. The overall financial benefit received by Winterflood from its trading in FEI shares was approximately £1.2 million, which exceeded the benefit received in respect of any other single security. Of this sum, the benefits largely resulted from trading with SP Bell: £191,000 in relation to the shares sold to SP Bell that were purchased from the two principal shareholders and £780,000 in relation to the rollover trades.
91. The suspension of trading in the shares on 15 July 2004 caused the unsettled positions in FEI shares at SP Bell to crystallise. Neither the clients of SP Bell nor SP Bell itself had sufficient funds to settle the resulting debt, which was over £9 million. SP Bell ceased trading and was placed into administration on 23 July 2004 and its business and assets were sold to another FSA authorised firm.

Winterflood - Summary of representations

General

92. Winterflood made written representations on 30 January 2008, 1 April 2008, 18 April 2008 and 23 April 2008 and oral representations on 2 and 3 April 2008. Winterflood also provided an opportunity for the decision-maker to view trading activity as it is now conducted by Winterflood's traders. To support its representations Winterflood provided reports of individuals with relevant experience.
93. Winterflood dispute the findings set out in the Warning Notice and any suggestion that they should be implicated in the deliberate scheme conducted by Simon Eagle through SP Bell. In particular the trading directors of Winterflood did not know details of the trading with SP Bell. Winterflood did not act recklessly, and did not fail to meet the standards of behaviour reasonably to be expected by a regular user of a market maker in AIM stocks. The Warning Notice does not have regard to certain important characteristics of the AIM market, namely the role of a market maker, its quotes, and relevant internal controls and procedures at Winterflood.

Legal interpretation of the market abuse regime

94. Winterflood argued that the legal approach that should be adopted would not justify a finding that it had engaged in market abuse. It argued that to establish market abuse involving price positioning and execution of artificial transactions, the FSA would need to establish that Winterflood itself had the purpose of carrying out an artificial transaction or positioning the price, and also to establish that Winterflood had acted with impropriety not merely failing to take due care to appreciate risks.
95. Winterflood accepts that intention to abuse the market does not need to be shown to establish market abuse. However, Winterflood argued that the Code of Market Conduct, given the statutory provisions giving rise to it, effectively incorporated a requirement for an actuating purpose for the kind of market abuse alleged against Winterflood in the Warning Notice. The provisions in the Code of Market Conduct stating that it is not (and not intended to be) exhaustive are to be read in the light of the relevant statutory provisions, and proper legitimate expectation, as covering wholly different types of behaviour amounting to market abuse. The Code should not be read as allowing the FSA to take action against Winterflood which did not have any actuating purpose.
96. Winterflood argued in similar fashion in relation to assessing standards of behaviour – that the FSA must establish that Winterflood engaged in improper conduct. It is not sufficient simply to establish that Winterflood failed to take reasonable steps to check the propriety of the trades, or failed to act with due skill care and diligence.

Characteristics of AIM and market making

97. Winterflood commented that AIM is a quote-driven market and a market maker is required to publish two-way prices for all stocks in which it makes a market, and to deal at those quoted prices in transactions up to its published "screen size" (the market

maker's quoted maximum size – which must be no smaller than the normal market size for the stock). The market maker is not obliged to deal in sizes larger than the screen size. A broker who wishes to do so will need to agree a price with the market maker for that trade. Because of the market maker's obligation to deal at his quoted prices the market can never be misled by its quotes. In addition other market makers are entitled to challenge a market maker to buy or sell at its quoted price. This and market reaction act as a check on the market maker's freedom to quote prices.

98. A market maker's published prices are not an indication of any objective value or price of the stock. They are merely the prices at which the market maker is prepared to buy or sell that stock in sizes up to the market maker's screen size, and the prices at which the market maker's traders subjectively believe will make money in the market. (The market maker is entitled to deal outside its quote for larger trades, particularly if it is taking risk.) The published prices may reflect matters known to the market maker but not in the public domain – for example a large purchase or sale which has yet to be effective. Different market makers may take different views or have different strategies and therefore publish different prices. Accordingly the published prices cannot be relied on as an accurate reflection of interest in the market or of supply and demand. The appropriate reflection is in the "touch price" (the spread between the best bid and best offer prices across all the market makers in the stock).
99. Although trade reports to the LSE include information about settlement dates this does not appear on the trade reporting screens. Therefore the reports seen by the market cannot mislead as to whether trades have settled or will settle, nor whether shares have been or will be paid for. Trade reporting screens do not provide any immediate or complete report of trades. They do not show whether trades are buys or sells, settlement dates, or disclose the counterparty; and there are legitimate trading reasons why the market is given incomplete information. The trade reporting screens are therefore not a reliable source of information and market users rely on experience to interpret the information shown.
100. Stocks on the AIM market tend to be more volatile than those on the main market – less information is required to be published and there is less publicly available information about issuers. Price movements can be very dramatic, particularly in "penny stocks", and can be the result of different reasons. A stock's price can increase by multiples very quickly. It is not uncommon for market participants to buy a stock because its price is rising.
101. Between July 2003 and July 2004 the AIM market rose on average by about 40%. Since a number of share prices did not move significantly, many rose by more than this proportion.
102. Reasonable market makers and participants in the AIM market, between July 2003 and July 2004, would not have been surprised that the price of an AIM stock such as FEI rose gradually over the period – even if the corporate activity (actual and prospective) of FEI and the press reporting of that activity did not provide apparent rational reasons for this. The rise of a share price from 2.5p to 11.5p over a year would not be regarded as out of the ordinary or requiring investigation by those responsible in a market maker for supervising trading.

The role of a trader

103. Winterflood stated that a “number one” trader is responsible for trading a “book” of about 200 AIM companies. Although there will not be active trading in all of those companies every day, a very substantial number of trades will be conducted on the “book”. (Winterflood provided examples of the number of bargains per trading day.)
104. An AIM trader does not have time to analyse each trade that he undertakes, will not remember the details of individual trades undertaken more than a few days previously (unless there is a particular reason for doing so), and will not be able from memory to conduct the kind of analysis that the Warning Notice suggests would have been conducted by a reasonable market maker.
105. Winterflood’s traders do not research the companies on their “book” or seek to understand the fundamentals of their businesses or their prospects. They do not seek to make money from taking positions in the stocks, and accordingly do not have an interest in the price of a stock. A market maker looks to provide liquidity to the market by offering to sell or buy at quoted prices. He looks to make money by making a “turn” on those trades. This is irrespective of the fundamental strength or weakness of the stock. Traders will not usually know the size of the issued capital and, therefore, not usually know what proportion of the issued share capital they are trading.
106. A trader has to judge the current and future supply and demand for a stock. The ideal conditions are where there are both buyers and sellers – to him an “orderly market” is a market in which the orders of both buyers and sellers can be satisfied. The trader will adjust his prices and spread to seek to achieve this. In doing so he will have regard to a number of things including what he knows but others do not about current and future demand, what he assesses to be the position of other market makers, the impact of reported trades, public statements by the company, press comment or rumour. A trader faced with an inactive market may move his quote to stimulate activity. Setting the market maker’s quote is not scientific and is very subjective to individual traders.
107. If asked to price a trade that is larger than the screen size, a trader will assess the risk of not being able to sell or buy those shares at a profit and the total financial exposure in respect of his total holding of those shares. If the risk is none/small or will not give an unacceptable financial exposure (e.g. he has a matching buyer or seller identified) he is likely to price within the touch and accept a smaller turn. If the risk is large he will typically look to price outside the touch to give himself the chance to make a bigger turn or smaller loss.
108. Discussions between market makers and brokers about demand and price are constant. Without them a trader would not have the information to enable him to exercise his judgment as to the prices to quote, and he would be risking capital “blind”. It is not uncommon for a trader to be contacted by a broker, with whom he deals regularly and who is interested in a stock, with a suggestion that the trader move his price. A suggestion from a broker, who is known to be close to a company or to deal regularly in its stock, is more likely to be taken seriously. When a broker, with whom the trader

deals regularly and has a relationship, suggests that a trader increases his quote, the express or implicit message to the trader is that the broker has buyers, that he wishes to attract sellers and that he will buy to the suggested price. If he does not, then the trader's trust will have been misplaced and there may be an impact on the relationship.

109. A trader cannot know the identity or intentions of the clients of brokers with whom he trades. He is not entitled to know the identity of the broker's client. He will never ask a broker who is dealing in a stock or why. The trader has to rely on the broker, which is always an FSA regulated entity, to satisfy itself about the identity, resources and intention of the broker's clients and the reasons for, or appropriateness of, their trades. Absent specific concerns a trader does not address his mind to these issues. He does not concern himself with settlement, and if no settlement issues arise with trades conducted through a regulated broker, there is no reason to question whether the trades are genuine.

Internal controls and procedures

110. Winterflood do not consider it possible or necessary to focus regular control and supervision of trading on individual trades. Instead risk control and supervision is aimed at ensuring that trades match and settle, making dealings transparent, and operating financial limits on trading positions. Winterflood's contemporaneous management control provided information about profits and losses, and would enable a director to identify where a particular "book" was making an atypical profit or loss. From there a director could go into further folders, and ultimately could go view a "trading folder" showing the trades for a particular stock. In the case of SP Bell trades, for the relevant period, the counterparty appeared on the relevant screens as Pershing, and was not separately identifiable. Since the problems emerged Winterflood has introduced new management information reports and provided details of these.

Impact of matters argued by Winterflood to have been accepted by the FSA

111. Winterflood argue that a number of matters accepted by the FSA fatally weaken the case against Winterflood:
 - 111.1 The rollover trades are said to be from one SP Bell client to another (see paragraph 40), so that in the absence of collusion (of which there is no evidence) there was no deferral of settlement and Rule 3050 has no application.
 - 111.2 The FSA accept that it was reasonable for Winterflood to assume that rollovers before 1 January 2004 were proper and genuine and complied with Rule 3050 (see paragraphs 43 and 46). If so, or if they were not conducted for the purpose of deferring settlement, there is no basis for suspecting that identical trades in early 2004 were conducted to defer settlement.
 - 111.3 If the rollover trades "were visible to the market" (accepted in the Enforcement team's original submissions document), the market was not

misled as to the nature and number of those trades, or as to the number or proportion of FEI shares being traded by rollovers.

111.4 The FSA accept (in the Enforcement team's original submissions document) that it was reasonable for Winterflood to believe that the rollover trades were being settled by SP Bell clients. If so, there is no basis for alleging that a reasonable market maker in Winterflood's position should have concluded that the trades were undertaken to defer settlement (in breach of Rule 3050) or that there was a risk that they were not proper and genuine, or that they were not being paid for.

Sale by the former directors of their FEI shares

112. Winterflood argued that the circumstances of the sale were not such that Winterflood should have been put on notice that the sale was unusual. Before July 2003, 85% of FEI shares were held by two shareholders who were not trading. Accordingly it is not surprising that trading was lower than when most FEI shares were available for trading, and for this reason alone increased trading after the sale was not suspicious. Also a typical consequence of a takeover of a company with little or no business activity (which FEI was before July 2003) is an increase, sometimes large, in trading volume and share price. It is not unusual and there may be good reasons for trades involving a large proportion of the issued stock to be undertaken with the involvement of a market maker. Winterflood and its traders did not know that Mr Eagle was receiving a commission from the sellers or was otherwise acting "on both sides of the sale".
113. Winterflood's traders understood that the transactions were not unusual in involving Winterflood. The initial surprise that the transaction was not being effected through an agency cross was based on a misunderstanding of the position that Mr Eagle knew both seller and buyer and SP Bell would be acting for both. Winterflood's traders believed that the sellers were using Mr Eagle to find buyers and that he was looking for buyers to support his plans for FEI. This size of sale is akin to a seller placing a large sell order with a market maker to fulfil. It is not surprising to use a market maker and sell the stock in tranches as he found buyers. The sale achieved an excellent result for the former directors.
114. Winterflood's involvement did not obscure the full extent of Mr Eagle's financial interest and involvement in the FEI share sale, nor did it allow him to conceal the fact that he stood to earn a significant commission from the sellers.

The rollover scheme

115. Winterflood argued that it and its traders were not aware nor would a reasonable market maker with their knowledge have been aware (before later in summer 2004) of any matters to alert them to the risk that the rollover trades were not proper and genuine trades. A market maker will often be unable to distinguish between trades between two clients of the same broker and a pair of trades involving the same client. Winterflood remains of the view that there was no breach of Rule 3050, and considers that the wrongdoing was SP Bell's trading without client authority. This is not

something that Winterflood or any other market maker could identify. The difference in settlement periods is not a clear indicator that trades are being undertaken to defer settlement – most of Winterflood’s AIM sale trades have a different settlement period compared with most of its buy trades.

116. Although the volume of shares being rolled over may have dwarfed the number of FEI shares being bought throughout the relevant period, and the volume and frequency of rollovers may have been highly unusual, but these matters were visible to the market, as was the fact that they were rollovers. The market was not therefore misled as to demand for FEI shares. Settlement dates are not reported to the market so the reporting did not conceal from the market that a significant amount of FEI shares had not been paid for (and in any event the shares had been paid for by whichever of Winterflood or Pershing was the purchaser).
117. Winterflood’s traders believed (and were entitled reasonably to believe) that there was a steady demand by SP Bell clients for FEI shares. Shares offered to SP Bell were bought, and settled. They also believed that the few requests by SP Bell traders to increase the FEI price were made in the ordinary course of communication between a market maker and a broker. They ignored some and used their judgement to act on others.
118. Winterflood do not accept that a market maker with the same knowledge as Winterflood’s traders should have seen a need to ask questions of SP Bell about the number of rollovers. If they had done so they would have had to take on trust the answers given, and the answers would have been likely to have been the same reassurance that another market maker may have received when it did ask (Winterflood does not accept that the other market maker did actually ask).

Constant source of buyers

119. Winterflood argued that its traders did not know that the SP Bell clients’ trading was unusual. There are other potential explanations for the matters relied on in the Warning Notice. A trader is unable to identify the client of the broker or the reasons for trading by that client. A broker will have discretionary mandates and where it does not it may obtain broad instructions from its client. The trader does not address his mind to these matters when executing a trade.
120. Simon Eagle’s dual role with SP Bell and FEI did not, of itself, give rise to a conflict of interest, though there was a potential conflict of interest in that situation. Such conflicts are not uncommon and are not something which a market maker can address. The market maker does not have any obligation to act in the best interests of SP Bell’s clients. He would not know the identity, financial circumstances, investment objectives or other client specific matters. Winterflood’s traders believed, reasonably, that there was a constant demand by clients of SP Bell for FEI shares.

Delayed rollovers

121. Winterflood accepted that delayed rollovers are rare. It does not follow that they are always improper or mislead the market or that a market maker asked to undertake

them should be suspicious as to possible wrongdoing. They are rare because the market maker is exposed to a risk that the broker will not complete the second leg, and receives no recompense for carrying this risk. They are capable of being for legitimate reasons.

122. Both legs of all the delayed rollovers were conducted within Winterflood's quote and the market touch price. Regular users would likely have assumed that each leg was low risk for Winterflood. Given the size regular users would likely also have assumed that they were one leg of a matched trade. Similarly they would likely also see a number of shares reported at the same date and time as being part of a matched trade. Where delayed rollovers were transacted at the top end of the touch price regular users would not necessarily have assumed that they represented actual or potential buying interest, or any conclusions. The volume of the delayed rollovers was not so large, compared with the volume involved in rollovers in 2003 and up to March 2004 as to give rise to suspicion. Even if Winterflood traders had asked questions it would have served no purpose.
123. Winterflood did not decide not to execute further delayed rollovers in FEI. A Winterflood trader decided that he was uncomfortable accepting requests from SP Bell for delayed rollovers in another stock. No requests for delayed rollovers in FEI were received from SP Bell after that.

Involvement of Winterflood directors

124. Winterflood accepted that the two trading directors did review trading on the books run by Mr Sotiriou and Mr Robins. Review of trading in a particular stock would only have been possible at a level which would only have been done if higher levels of review indicated an abnormality of trading or an issue that needed research. The trading directors do not recall regularly reviewing FEI trading and based on the information available to them at the time do not now consider that it would have caused them to do so. The indicators do not suggest excessive trading or excessively profitable trading.
125. If the trading directors had had any concerns about trading in FEI shares they would have raised questions of Mr Sotiriou or Mr Robins. They did not. Had they done so they would have learned of the matters which those traders were aware of and believed. That would not have alerted them or the directors of a reasonable market maker to raise questions of SP Bell. The directors were not aware of the trading in FEI shares of SP Bell clients until June 2004. Paragraph 75 of the Warning Notice does not accurately reflect the conversation concerned. This related only to the credit risk taken by Winterflood in carrying out "lopsided put-throughs".

Manipulation of the share price

126. Winterflood stated that it and its traders were not aware of Mr Eagle's rollover scheme or that he needed continued increases in the share price to continue it. They were also unaware of the matters set out in paragraphs 77 to 79 of the Warning Notice. Winterflood did not give knowing cooperation to Mr Eagle's share price manipulation scheme and did not knowingly execute rollover and delayed rollover

trades as part of that scheme. Senior management's decision to continue delayed rollover trades was taken solely on the grounds of lack of credit risk. Winterflood's increases in its bid/offer quotes was not to cooperate with improper conduct by SP Bell or Mr Eagle. Winterflood does not accept that on any of the 15 occasions identified by the FSA its increases in its quote lacked independent judgment, were improper, or can otherwise be criticised. These increases did not cause the FEI price to be artificially high if (as appeared to be the case to Winterflood) the SP Bell trades were genuine.

Concluding remarks

127. Winterflood argued that it did not fail to satisfy the standards of behaviour reasonably to be expected of a market maker in AIM shares, in the prevailing circumstances and with the knowledge that Winterflood had. There is no basis for the allegation that Winterflood engaged in market abuse – there is no basis to conclude that Winterflood and its traders behaved contrary to s118, nor any basis for concluding that there was the requisite knowledge on the part of Winterflood (as opposed to its traders) to establish market abuse by Winterflood. There is no justification for a case of recklessness or knowing disregard or of deliberate closing of minds to clear and substantial risks.
128. Winterflood has cooperated fully with the FSA's inquiry into FEI trading, and has taken steps to improve its systems and controls (which it accepts might have constituted a breach of FSA Principle 3 for businesses). Winterflood accepts that had they, in 2004, had the management systems and reports that they now have, the scale and nature of SP Bell's trading would have come to the attention of Winterflood's trading directors and would have provided with material necessary properly to challenge the trading. Any such shortcomings do not amount to market abuse.
129. A number of "benefits" said to have been received by Winterflood are not properly regarded as benefits. In addition Winterflood has more than disgorged any benefit from its trading with SP Bell in its settlement of claims by Pershing. In addition the matters suggested to be aggravating factors ought not be taken into account in considering any penalty. In particular it is inappropriate to attribute SP Bell and Mr Eagle's wrongdoing to Winterflood and to apportion blame to Winterflood for it.

Winterflood - Conclusions

Summary

130. In summary the FSA is satisfied that Winterflood's behaviour in continuing to execute trades, in particular the rollover and delayed rollover trades in the relevant period, in the context of the overall pattern of trading amounted to market abuse. However, the FSA is not satisfied that Winterflood's involvement in Mr Eagle's share price manipulation scheme amounts to market abuse by Winterflood.

Legal interpretation and the standard of behaviour expected of Winterflood

131. The FSA does not accept that the Code of Market Conduct should be read in the way contended by Winterflood. The FSA's view is that it is required to apply the statutory test required by section 118 of the Act in each individual case. The Act specifies that the Code "may be relied on so far as it indicates whether or not that behaviour should be taken to amount to market abuse" (section 122(2) of the Act). The FSA considers that this makes plain that the Code cannot have effect beyond this so as to supplant the statutory test in any way. The Code (except to the extent that it identifies behaviours that the FSA considers not to be market abuse) is properly considered as no more than an aid to interpreting the statutory provisions. This is reflected in the provisions of the Code that emphasise that it is not (and could not be) exhaustive as to what is and is not properly to be considered market abuse.
132. Accordingly, the FSA does not accept Winterflood's representations as to the interpretation of the market abuse regime. The FSA notes that the training on the introduction of the market abuse regime provided to Winterflood employees acknowledges that the proper approach is to apply the statutory tests in each case, and also that the Code of Market Conduct is not exhaustive.
133. The FSA notes that the relevant Code of Market Conduct states that a "mistake is unlikely to fall below the objective standards expected where the person in question has taken reasonable care to prevent and detect the occurrence of such mistakes" (MAR 1.2.6E). The FSA considers that this makes clear that mistakes or other failures to take care can amount to market abuse if the person concerned has not taken reasonable care to prevent and detect such mistakes or failures to take care. The FSA accordingly does not accept that impropriety is required before concluding that behaviour amounts to market abuse. The only relevant test is that specified in section 118 of the Act of whether the relevant behaviour amounts to a "failure ... to observe the standard of behaviour reasonably expected of a person in [Winterflood's] position in relation to the market".
134. The Code of Market Conduct identifies the extent of compliance with relevant rules and regulations of the market in question as a factor in determining whether or not behaviour falls below the standards expected. The FSA therefore considers that the key aspects of the behaviour to be expected of a market maker in Winterflood's position are to be derived from the relevant rules of the London Stock Exchange (LSE) (of which both Winterflood and SP Bell were, at the relevant times, members) that were discussed during the making of representations, and, in particular, from rule 3300:

"3300 A member firm shall not, in respect of its on Exchange business:

3300.1 do any act or engage in any course of conduct which creates or is likely to create a false or misleading impression as to the market in, or the price or value of, any security;

3300.2 cause or enter into any artificial transaction;

...

3300.6 do any act or engage in any course of conduct which causes, or contributes to, a breach of the Exchange's rules by another member firm."

135. Accordingly, the FSA considers that a regular user of the AIM market expects a market maker to comply with LSE rules, so that if it works closely with brokers (particularly when illiquid stock is involved) it will take reasonable care in doing so. In particular, a regular user would expect that a market maker will not contribute to a broker creating or being likely to create a false or misleading impression as to the market in, or the price or value of, any security, or to a broker causing or entering into any artificial transaction. The FSA further considers that a regular user would expect a market maker to take reasonable care in its relationship with brokers in order to maintain an appropriate standard of behaviour.

The context for the trades conducted by Winterflood

136. The FSA is satisfied that by 5 January 2004, Winterflood knew or ought reasonably to have concluded that:
- (1) As a result of the initial sale referred to in the Warning Notice, Mr Eagle was in the very unusual position of having effective control of and being senior executive of both an AIM quoted company, and a stockbroking firm;
 - (2) Mr Eagle was, apparently, able to commit SP Bell clients to transactions without seeking their specific instructions;
 - (3) Mr Eagle preferred to discuss all matters, including those relating to trading by SP Bell in a quoted company controlled by him (in which he had a personal financial interest and in relation to which he had an inevitable conflict of interest) on untaped lines – in particular preferring to discuss matters in mobile to mobile telephone conversations; and
 - (4) SP Bell had already conducted a very significant volume of trading in FEI shares, including very large rollover trades (see, in particular, paragraphs 41 and 42).
137. The FSA is satisfied that by January 2004, Winterflood knew or ought reasonably to have concluded, in relation to the standards of behaviour reasonably expected of a market maker, that:
- (1) Mr Eagle's unusual position would inevitably present him with a conflict between his personal interest in seeing an increasing FEI share price and his responsibility to act in his clients' best interests by advising his clients at some point to realise profits by selling shares (which would potentially depress the FEI share price);
 - (2) Mr Eagle's apparent desire for his conversations to be conducted on mobile telephones by him and by Mr Sotiriou indicated a risk of impropriety;

- (3) Mr Eagle's apparent authority to commit SP Bell clients to trades gave rise to the risk that he would use rollover transactions between client accounts to breach rule 3050 or to undermine its purpose;
 - (4) There was a risk that the high volume of rollover transactions, representing an unusually high turnover of the issued share capital, of one stock were not genuine and proper;
 - (5) In the light of that risk, high volumes of rollover transactions were capable of giving a false impression to the market as to the supply of, or demand for, the shares concerned;
 - (6) Repeated delayed rollovers/put-throughs are highly unusual and, though individual delayed rollovers/put-throughs are capable of innocent explanation, had a strong potential to give misleading impressions to the market as a result of the differences in timing between the legs of the transaction;
 - (7) As a consequence, delayed rollovers involved risks beyond the immediate one of whether the second leg of the transaction would actually be executed by the counterparty; and
 - (8) Settlement of transactions of itself is not conclusive as to propriety of those transactions.
138. It is not necessary for each or any of these matters, individually, to justify giving rise to suspicion. However, the cumulative effect of these matters was the context within which Winterflood, through its traders, acted as it did.
139. Between 5 January and 14 July 2004 the rollovers (including delayed rollovers) continued to present alerting factors to Winterflood.

Winterflood's behaviour

140. The FSA accepts that the available evidence does not provide sufficient basis to conclude that Winterflood positioned the share price of FEI at an artificially high level as suggested in the Warning Notice.
141. However, the FSA is satisfied that a regular user would regard Winterflood's behaviour as a failure to observe the standard of behaviour reasonably expected (being the duty described above, including the duty to act in accordance with LSE rules), in continuing to execute large numbers and volumes of rollover trades between 28 January 2004 and 14 July 2004, and in executing delayed rollovers between 5 January and 18 March 2004.
142. The FSA is satisfied that a regular user would reasonably expect that in the context described above Winterflood would review its relationship with SP Bell and Mr Eagle and use available lines of enquiry to seek to check the propriety of the trading, including questions of SP Bell and/or Pershings. The FSA is also satisfied that the regular user would have formed that view at the time of the behaviour in question.

143. The FSA considers that Winterflood's behaviour amounted to a course of conduct contrary to relevant standards reflected in LSE rule 3300, in that it:
- (1) created or was likely to create a false or misleading impression as to the market in, or the price or value of, FEI shares; and
 - (2) contributed to a breach of LSE rules by SP Bell (another LSE member), being the market abuse conducted through SP Bell by Mr Eagle.
144. The FSA considers that Winterflood's behaviour contributed to a serious case of market abuse (i.e. deliberate share price manipulation by Mr Eagle), as a result of Winterflood's continuing failure to identify the need to assess its relationship with SP Bell and Mr Eagle, involving reliance only on the fact that Winterflood's transactions settled with Pershing and (in relation to the delayed rollover trades) identifying only the risk that the second leg of the trade would not be executed.
145. As the leading market maker for FEI shares, Winterflood ought to have recognised its responsibilities to the market and the particular risks to its responsibilities arising in a close relationship with the dominant broker in those shares. It did not do so and did not, having only one member of staff responsible for compliance matters, adequately organise itself to be able to do so. Winterflood's trading was pivotal to the operation of Mr Eagle's share price manipulation scheme (even though that scheme was not shared by Winterflood). Whether or not Winterflood acted recklessly, its behaviour should be regarded as serious and the FSA has decided to impose a substantial financial penalty to reflect that.

Financial Penalty

146. Section 124 of the Act requires the FSA to issue a statement of its policy with respect to the imposition of penalties for market abuse and the amount of such penalties. The FSA's policy in this regard is contained in Chapter 6 of the Decision procedure and penalties manual (DEPP). In deciding whether to exercise its power under section 123 of the Act in the case of any particular behaviour, the FSA must have regard to the policy set out in DEPP 6.
147. The FSA has decided to reduce the financial penalty compared with that proposed in the Warning Notice dated 18 October 2007. This reflects, in particular, the impact of its conclusion that it is not satisfied that Winterflood artificially positioned the price of FEI shares.

Decision Procedure and Penalties Manual

148. DEPP 6.2 sets out a number of factors to be taken into account when the FSA decides to take action, including for behaviour appearing to be market abuse. They are not exhaustive, but include the nature and seriousness of the behaviour in question, the conduct of the person concerned after the behaviour was identified, the degree of sophistication of the users of the market in question, the size and liquidity of the market and susceptibility of the market to market abuse. Other factors also include action taken by the FSA in similar cases, the impact that any financial penalty

or public statement may have on the financial markets or on the interests of consumers, and the disciplinary record and general compliance history of the person.

149. In enforcing the market abuse regime, the FSA's priority is to protect prescribed markets from any damage to their fairness and efficiency caused by the misuse of information in relation to the market in question. Effective and appropriate use of the power to impose penalties for market abuse will help to maintain confidence in the UK financial system by demonstrating that high standards of market conduct are enforced in the UK financial markets. The public enforcement of these standards also furthers public awareness of the FSA's protection of consumers' objective, as well as deterring potential future market abuse.
150. In accordance with the FSA's published policy in determining whether to take action in respect of market abuse and in determining the level of financial penalty imposed, the FSA will take into account all the circumstances of a particular case. These include the need to deter such behaviour, the nature and seriousness of the abuse, the person's conduct following the abuse (including their co-operation with the FSA's investigation), the nature of the market that has been abused, the likelihood of behaviour of the same type being repeated and the previous history of the person concerned.
151. The FSA has taken all the circumstances of this case into account in deciding that it is appropriate to take action for behaviour amounting to market abuse, that the imposition of a financial penalty in this case is appropriate, and the level of the penalty imposed is proportionate. The FSA has had particular regard to the guidance set out in DEPP 6. In particular the FSA considers the following aggravating and mitigating factors to be relevant:

Aggravating features

- 151.1 The gravity of the offence: the market abuse continued over a sustained period, and had the impacts described below.
- 151.2 Whether the offence was deliberate or was committed through inadvertence: Winterflood failed to consider and address the clear and substantial risks that the rollovers and delayed rollovers were not proper and genuine trades; that the apparently unlimited demand for FEI shares from SP Bell clients was not genuine; and that its trading was assisting in Mr Eagle's share price manipulation scheme. Such behaviour fell far below the standard of a reasonable market maker.
- 151.3 Impact of the behaviour on prescribed markets: Mr Eagle's scheme was a classic share ramping scheme. As such, it clearly had the potential to cause serious loss to investors and to damage confidence in the AIM market. In general, market abuse seriously undermines investor confidence and affects the fair and orderly operation of markets. Winterflood's conduct misled the market and assisted Mr Eagle's scheme, which ultimately caused a substantial potential and actual loss to retail investors.

151.4 Winterflood received an estimated financial benefit of £900,000 from its trading.

151.5 Directors of Winterflood were directly involved in approving the trading and allowing it to continue.

Mitigating features

151.6 Winterflood has co-operated with the FSA's investigation;

151.7 There have been no previous findings of market misconduct against Winterflood; and

151.8 Winterflood has, since the matters described in this Notice have come to light, put in place changes to its systems and controls. It has an enhanced training programme for its traders, enhanced post-deal compliance monitoring, a report comparing trading and physical stock positions, intra-day exposure limits, and additional Board Reports.

152. As a matter of principle, the financial benefits which Winterflood received should be disgorged.

153. In determining the proposed financial penalty the FSA has considered the financial benefits received by Winterflood and the need to punish Winterflood and deter Winterflood and others from engaging in this type of activity. The FSA has also had regard to penalties imposed in other market abuse cases.

Sanction

154. Pursuant to section 123 of the Act, the FSA has taken all of the relevant circumstances into account in deciding that Winterflood has engaged in market abuse. As a consequence of its conclusions, the FSA has decided to impose a financial penalty of £4 million.

155. The financial penalty consists of the following elements:

(1) a disgorgement of estimated financial benefits arising from the market abuse of £900,000;

(2) an additional penalty to make up a total penalty of £4 million.