Financial Conduct Authority

FINAL NOTICE

To:	**David Gillespie**	**To:**	**Pritchard Stockbrokers Limited (In Special Administration)**
IRN:	**DJG01107**	**FRN:**	**124257**
Date of Birth:	**2 December 1948**		
Date:	**9 October 2014**		

ACTION

1. For the reasons given in this notice, the Authority hereby:

   a) imposes on David Gillespie a financial penalty of £10,500 for breaches of Statements of Principles 1 and 6, pursuant to section 66 of the Act;

   b) withdraws the approval given to Mr Gillespie to perform controlled function CF1 Director at Pritchard, pursuant to section 63 of the Act; and

c) makes an order prohibiting Mr Gillespie from performing any function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm, pursuant to section 56 of the Act.

2. Mr Gillespie agreed to settle at an early stage of the Authority's investigation. He therefore qualified for a 30% discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £15,100 on him.

3. Mr Gillespie provided verifiable evidence of serious financial hardship. Had it not been for his reduced financial circumstances, the Authority would have imposed a financial penalty of £144,000 (or £100,800 adjusted for a 30% discount if settled early).

SUMMARY OF REASONS

4. Mr Gillespie breached Statement of Principle 1 during the Relevant Period by failing to act with integrity in that he recklessly failed to provide adequate protection for client monies for which he, as the Managing Director and the CF10a holder at Pritchard, was ultimately responsible. Mr Gillespie was personally culpable as he recklessly relied upon the existence of an undocumented and opaque Offshore Facility in attempting to correct a deficit which Pritchard had wrongfully brought about in its client money resource. He wrongfully included the Offshore Facility as an available client money resource when reconciling the amount of client money that needed to be segregated by Pritchard. This failure contributed to a loss of approximately £3 million to Pritchard's clients by the time Pritchard entered into Special Administration.

5. Mr Gillespie had the primary contact with the overseas company providing the Offshore Facility and he assured his fellow director, David Welsby, the Finance Director with responsibility for accounting and performing the internal reconciliation of client money, of the existence of the Offshore Facility.

6. As a consequence of Mr Gillespie's failings as set out in paragraphs 4 and 5 above:

a) client money was wrongly used to pay business expenses;

b) Pritchard failed to routinely pay sufficient funds into its client bank account to cover shortfalls in client money, in breach of the Client Money Rules;

c) Pritchard placed reliance upon the Offshore Facility when calculating the client money resource for inclusion within Pritchard's internal reconciliation of client money, despite the fact that such a facility was not permitted to be included in the resource in accordance with the Client Money Rules; and

d) the Authority was not informed when the shortfalls could not be rectified immediately.

7. Further, despite becoming aware on or before 7 February 2012 that the funds were not available to Pritchard, but were instead conditional on an agreement being made with the overseas company providing the facility, Mr Gillespie:

a) advised Mr Welsby that the Offshore Facility qualified as client money, with the result that an entry into Pritchard's accounts was made on 8 February 2012 showing funds being available in cash to cover the client shortfall, even though Mr Gillespie was aware, or became aware on 7 February 2012, that the release of funds from the Offshore Facility was conditional on an agreement being made with the overseas company providing the Offshore Facility, and

b) failed, at a meeting with the Authority on 8 February, to advise the Authority of the conditional nature of the Offshore Facility, with the Authority instead being advised at the meeting that the Offshore Facility was available to cover any shortfall in the client funds.

8. In addition, Mr Gillespie breached Statement of Principle 6 by failing to exercise due skill, care and diligence when providing oversight of CASS matters at Pritchard. In particular, he:

a) accepted, on 11 November 2011, approval as Pritchard's CF10a without endeavouring to understand the serious responsibilities that the role conferred, and then failed to remedy that lack of understanding thereafter; and

b) failed in his role as CF10a to exercise adequate oversight of the operational effectiveness of Pritchard's systems and controls that were designed to achieve compliance with CASS, including but not limited to appropriate notification of misuse of client money and a failure to rectify client money shortfalls.

9. The Authority is not alleging or implying that Mr Gillespie acted dishonestly when it uses the term 'reckless' in relation to the failings detailed in this notice. The Authority considers Mr Gillespie's failings to be serious for the following reasons:

   a) these failings resulted in significant consumer detriment including contributing to a loss of approximately £3 million of client money;

   b) the failures directly led to Pritchard breaching the Client Money Rules and Principle 10 throughout the Relevant Period;

   c) the failures resulted in the FSCS having to compensate clients; and

   d) the failures led to Pritchard's books and records being inaccurate and therefore increased the cost of the Special Administration.

10. This action supports the Authority's operational objectives of securing an appropriate degree of protection for consumers and protecting and enhancing the integrity of the UK financial system.

DEFINITIONS

11. The definitions below are used in this Final Notice:

"the Act" means the Financial Services and Markets Act 2000;

"the Authority" means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority;

"CASS" means the Client Assets Sourcebook contained in the Authority's Handbook;

"Client Money Rules" means Chapter 7 of CASS (as defined above);

"CF10a" means an individual approved by the Authority (as defined above) for the CASS operational oversight function;

"DEPP" means the Authority's Decision Procedure & Penalties Manual;

"EG" means the Enforcement Guide;

"FSCS" means Financial Services Compensation Scheme;

"Principle 10" means Principle 10 of the Authority's Principles for Businesses;

"the Offshore Facility" means the undocumented £2 million overdraft facility purportedly provided by an offshore company;

"Pritchard" means Pritchard Stockbrokers Limited;

"Relevant Period" means 1 July 2010 to 8 February 2012;

"Statements of Principle" means the Statements of Principle for Approved Persons;

"Special Administration/ Special Administrators" refers to the regime governed by the Investment Bank Special Administration Regulations 2011; and

"the Tribunal" means the Upper Tribunal (Tax and Chancery Chamber).

FACTS AND MATTERS

Background

12. Pritchard was incorporated in England and Wales on 14 April 1986 and authorised on 1 December 2001 to carry on designated investment business. Mr Gillespie was approved as a Director (CF1) of the firm at its authorisation and had ultimate responsibility for the firm throughout the Relevant Period.

13. Pritchard's annual accounts for 2010 described its principal activities as that of "providing securities and financial advice and providing securities and dealing facilities on an agency basis." The structure of its business required it to be able to hold client money. It was authorised to do so in relation to the business it conducted through its headquarters in Bournemouth and 10 ancillary offices.

14. Pritchard had been experiencing financial problems since 2009. These financial problems put pressure on Pritchard's capital adequacy and client money positions. Mr Gillespie claims that he sought support from a trading counterparty of Pritchard via an offshore company, which purportedly offered an undocumented £2 million Offshore Facility to support Pritchard's client money position.

15. On 10 February 2012, due to concerns about Pritchard's holding of client money, the Authority secured Pritchard's assets and imposed a requirement on it to close out transactions it had already commenced.

16. On 9 March 2012, Pritchard entered Special Administration. It is estimated that Pritchard should have held an estimated £26.5 million in client money, approximately £3 million of which was represented by guarantees and the Offshore Facility purportedly provided by third parties that were irrecoverable or unenforceable, which caused the shortfall.

Internal reconciliation of client money

17. Pritchard followed, under the direction of Mr Welsby, its Finance Director, what is known as the standard method of internal reconciliation of client money. This is set out at Annex 1 to the Client Money Rules and requires, on each business day, a firm to conduct a reconciliation to check whether its client money resource was at least equal to its client money requirement at the close of the previous day in order to ensure that it has sufficient client money to repay what it owes its clients. In the event that the client money resource is insufficient to meet the requirement, the firm is obliged to transfer funds from its own resources to its client bank account(s) to cover any shortfall on the same day. If for any reason a firm cannot do this it is obliged to inform the Authority in writing, without delay.

18. The internal reconciliation of client money was carried out at Pritchard on a daily basis in line with the guidance in Annex 1 to the Client Money Rules. However, on days where Pritchard did not have adequate financial resources in its own account to cover the shortfall in the client account identified by the internal reconciliation of client money, a note was kept of the outstanding amount to be transferred. These amounts were initially recorded in manuscript, and then latterly electronically, in daily diaries.

19. In the course of the Relevant Period these daily diaries showed, with the exception of two days, client money shortfalls ranging between £198,000 and £2,676,252.

20. Pritchard, in breach of its regulatory duty, did not at any time in the Relevant Period inform the Authority of the shortfalls in its client money nor did it make good the shortfalls. Mr Gillespie, a chartered accountant and Managing Director, holding the CF3 Chief Executive function from 11 November 2011 until 6 March 2012, and (for the final three months of the Relevant Period) the CF10a of Pritchard, and the person at Pritchard who had primary contact with the overseas company which provided the Offshore Facility, was ultimately responsible for this failure.

Steps taken by Mr Gillespie to safeguard Pritchard's client money: the Offshore Facility

21. Mr Gillespie was aware of Pritchard's client money shortfalls and deteriorating financial position, looking as he did at the company accounts on a monthly basis. He relied on the supposed support he believed was offered by the Offshore Facility to cover the shortfalls in the client money resource. He described the support as being in the form of a facility or an overdraft facility that was held with a UK law firm in an escrow account on behalf of an overseas company, and was available to Pritchard on demand and free of lien.

22. The Client Money Rules do not recognise escrow accounts with law firms as being accounts into which client money can be deposited. Therefore, even if money had been ring-fenced in such an account, and there is no evidence that was the case, it could not have been designated as client money by Pritchard when calculating its client money resource in accordance with the Client Money rules.

23. Mr Gillespie had the primary contact with the overseas company providing the Offshore Facility. He conducted negotiations with the contacts responsible for the Offshore Facility, principally through telephone calls and meetings, of which there is no documentary evidence. Mr Gillespie nevertheless assured Mr Welsby of the existence of the Offshore Facility.

24. Neither Mr Gillespie nor Pritchard's other officers, staff or professional advisers have been able to provide any credible evidence of the existence of the Offshore Facility.

25. Mr Gillespie, as the primary point of contact with the overseas company which provided the Offshore Facility, failed to obtain or to put in place any contractual documents which would have enabled Pritchard to evidence or confirm the Offshore Facility. Instead, he relied on verbal assurances purportedly provided by and on behalf of the third party providing the Offshore Facility, and which he interpreted as meaning that the Offshore Facility existed and was available to be used by Pritchard.

26. Mr Gillespie accepted that there was an absence of paperwork to evidence the Offshore Facility and that he had, alone, negotiated on behalf of Pritchard, acknowledging that "it all sounds so horribly woolly with hindsight".

27. The absence of any documentary or other substantive evidence regarding the negotiation for the facility, whether in the form of communications with the overseas company or internally within Pritchard is very serious. It was compounded throughout the Relevant Period, by Pritchard's worsening financial position and the fact that Mr Gillespie knowing this failed to obtain from the overseas company legally binding documentation regarding the Offshore Facility. The absence of documentation was, he said, "a continuing topic of conversation" in Pritchard. In the circumstances, Mr Gillespie's failure to resolve or even address the problem was reckless. The Authority notes that Pritchard did not call upon the Offshore Facility at any time in the Relevant Period. Mr Gillespie believed without any proper basis for that belief that Pritchard's client money was not endangered at any point. Mr Gillespie accepted that "there has been a systematic failure within the firm." That failure contributed to the unsecured deficit of more than £3 million in Pritchard's client money account leading to actual customer detriment and the ultimate collapse of Pritchard.

Mr Gillespie's awareness that the Offshore Facility was conditional

28. Mr Gillespie was, or became, aware on 7 February 2012 that the release of the funds held pursuant to the Offshore Facility was conditional on an agreement being made with the Overseas Company providing the Offshore Facility. In particular, following a telephone conversation with a solicitor acting for the Overseas Company on 7 February, Mr Gillespie sent an email to the solicitor stating "*I share your reservations concerning the conditional aspect of the funds*", and subsequently sent an email setting out his understanding that the release of the funds was subject to the negotiation of a deal between Pritchard and the Offshore Company. Mr Gillespie advised Mr Welsby on 7 February that the funds were available and inaccurately stated that they did qualify as client funds, and did not advise Mr Welsby that the release of the funds was conditional. This led to an incorrect entry being made on 8 February 2012 into the Pritchard internal reconciliation of client money to show that the firm had funds available in cash to support the client money shortfall.

29. Furthermore, during a meeting on 8 February 2012 between Pritchard and the Authority, when the entry in the accounts showing funds available to cover the client shortfall was queried, Mr Gillespie did not advise the Authority of the conditional nature of the Offshore Facility, with the Authority instead being advised that the Offshore Facility was available to cover the shortfall in client funds.

Mr Gillespie's appreciation of client money issues

30. On 20 March 2009, the Authority sent letters to compliance officers of all firms with permissions to hold client money, including Pritchard. These letters made clear the Authority's concerns about firms' CASS compliance and set out the Authority's expectations of firms when arranging adequate protection for clients' assets and money.

31. On 19 January 2010, the Authority sent letters to all Chief Executive Officers of firms with permission to hold client money, including Pritchard. These letters emphasised that the Authority was giving a higher priority "to achieving compliance with client asset requirements" because it was concerned that firms were "not always achieving an adequate level of protection". The letters enclosed a report which noted that the Authority considered compliance with the Client Money Rules to be poor across the financial services industry. At the commencement of and throughout, the Relevant Period, Mr Gillespie therefore had or should have had a heightened awareness of the importance of affording adequate protection to client money and the concerns of the Authority in this respect. The onus was on Mr Gillespie and Pritchard to ensure that Pritchard paid heed to the Authority's concerns and acted upon them.

32. Further to the receipt of the letters to Chief Executive Officers, Mr Gillespie, as Pritchard's managing director, wrote to the Authority on 30 June 2010 to confirm that Pritchard's directorship had "properly considered the contents of the [Dear CEO] letter…". He added, "I further confirm that the firm is in compliance with its obligations for client money and assets". Having made such assertions in response to the Authority's letters, Mr Gillespie should have known that the Offshore Facility could not have been included as an available resource in its calculation of the client money resource.

33. In October 2010, and following consultation, the Authority announced its intention to introduce the CF10a controlled function because of the need to combat the fragmentation of CASS operational oversight in firms. Just over a year later, on 11 November 2011, Pritchard appointed Mr Gillespie to the role without undertaking any assessment of his knowledge or suitability for it. In interview, Mr Gillespie said that he assumed the role because he was asked to do so by the firm's directorship. He had no knowledge of it being a newly created controlled function, nor that it specifically entailed assuming responsibility for CASS oversight. It did not, he considered, add to the responsibilities he ordinarily

undertook. Mr Gillespie accepted that he should have made efforts to understand what the role of a CF10a entailed.

34. Individuals with approval to perform controlled functions, and in particular those involving the exercise of significant influence, must ensure that they understand their regulatory obligations in order to be able to discharge them adequately and thereby ensure the safe and compliant operation of the firm for which they are responsible. This is necessary to safeguard the interests of consumers and the market generally. Mr Gillespie did not understand and failed to take any steps to understand his responsibilities as CF10a.

FAILINGS

35. Based on the facts and matters described above, the Authority considers that in the Relevant Period Mr Gillespie failed to act with integrity in breach of Statement of Principle 1, and without due skill, care and diligence in breach of Statement of Principle 6. The regulatory provisions relevant to this Final Notice are referred to in the Annex.

Statement of Principle 1

36. Mr Gillespie breached Statement of Principle 1 by failing to act with integrity in that he recklessly failed to provide adequate protection for client monies for which he, as the Managing Director, the CF10a of Pritchard, and the person at Pritchard who had primary contact with the overseas company providing the Offshore Facility, was ultimately responsible. In the Relevant Period, he recklessly relied upon the existence and availability of an undocumented overdraft or financial facility, and which basic and obvious enquiries would have shown to be without substance, to support Pritchard's client money resource. His failure adequately to manage Pritchard's client money throughout the Relevant Period contributed to a loss of approximately £3 million of Pritchard's client money by the time Pritchard entered into Special Administration. As a consequence of Mr Gillespie's failings in relation to the Offshore Facility:

a) client money was wrongly used to pay business expenses;

b) Pritchard failed to pay sufficient funds into its client bank account to cover shortfalls in client money, in breach of the Client Money Rules;

c) Pritchard placed reliance upon the Offshore Facility when calculating the client money resource for inclusion within Pritchard's internal reconciliation

of client money despite the fact that such a facility was not permitted to be included in the client money resource in accordance with the Client Money Rules; and

d) the Authority was not informed when shortfalls could not be immediately rectified.

37. Further, Mr Gillespie breached Statement of Principle 1 in that, despite becoming aware on or before 7 February 2012 that the funds were not available to Pritchard, but were instead conditional on an agreement being made with the overseas company providing the facility, he:

a) advised Mr Welsby that the funds qualified as client money, and did not correct this; and

b) allowed the Authority to be advised by Pritchard, at a meeting on 8 February 2012, that the funds qualified as client money, before subsequently advising that the funds were in fact guarantees. In both cases this was inappropriate, inaccurate and misleading.

Statement of Principle 6

38. Mr Gillespie breached Statement of Principle 6 by failing to exercise due skill, care and diligence when providing oversight to CASS matters at Pritchard. In particular, he:

a) accepted the CF10a function, on 11 November 2011, without endeavouring to understand the serious responsibilities that the role conferred and then failed to remedy that lack of understanding thereafter; and

b) failed in his role as CF10a to exercise adequate oversight of the operational effectiveness of Pritchard's systems and controls that are designed to achieve compliance with CASS, including but not limited to appropriate notification of misuse of client money and a failure to rectify client money shortfalls.

SANCTION

Financial Penalty

39. The Authority's policy for imposing a financial penalty is set out in Chapter 6 of DEPP. In respect of conduct occurring on or after 6 March 2010, the Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5B sets out the details of the five-step framework that applies in respect of financial penalties imposed on individuals in non-market abuse cases.

Step 1: disgorgement

40. Pursuant to DEPP 6.5B.1G, at Step 1 the Authority seeks to deprive an individual of the financial benefit derived directly from the breach where it is practicable to quantify this.

41. The Authority has not identified any financial benefit that Mr Gillespie derived directly from the breach.

42. Step 1 is therefore **£0**.

Step 2: the seriousness of the breach

43. Pursuant to DEPP 6.5B.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breach. That figure is based on a percentage of the individual's relevant income. The individual's relevant income is the gross amount of all benefits received by the individual from the employment in connection with which the breach occurred, and for the period of the breach.

44. The period of Mr Gillespie's breach was from 1 July 2010 to 8 February 2012. The Authority considers Mr Gillespie's relevant income for this period to be £120,000.

45. In deciding on the percentage of the relevant income that forms the basis of the step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 40%. This range is divided into five fixed levels which represent, on a sliding scale, the seriousness of the breach; the more serious the breach, the higher the level. For penalties imposed on individuals in non-market abuse cases there are the following five levels:

Level 1 – 0%

Level 2 – 10%

Level 3 – 20%

Level 4 – 30%

Level 5 – 40%.

46. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, and whether it was committed deliberately or recklessly. DEPP 6.5B.2G(12) lists factors likely to be considered 'level 4 or 5 factors'. Of these, the Authority considers the following factors to be relevant:

    a) Mr Gillespie was reckless in relying on an undocumented facility; and

    b) Mr Gillespie's failure to protect adequately client monies contributed to a £3,021,660 loss of Pritchard's client money.

47. The Authority also considers that the following factors are relevant:

    a) The loss outlined above was suffered by consumers, at least some of whom were individual (i.e. non institutional) investors. The FSCS has confirmed that there are a number of consumers who have not been fully compensated due to their investments being for amounts higher than the FSCS £50,000 claim payment threshold; and

    b) Detriment has been caused to consumers as Pritchard remains in Special Administration and distributions to creditors, including claimants through the FSCS, have yet to be completed.

48. Taking all of these factors into account, the Authority considers the seriousness of the breach to be level 5 and so the Step 2 figure is 40% of £120,000.

49. The Step 2 figure is therefore **£48,000**.

Step 3: mitigating and aggravating factors

50. Pursuant to DEPP 6.5B.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including any amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breach.

51. The Authority considers that there are no mitigating or aggravating features.

52. The Step 3 figure is therefore **£48,000**.

Step 4: adjustment for deterrence

53. Pursuant to DEPP 6.5B.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the individual who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.

54. The Authority does consider the penalty against Mr Gillespie to be insufficient and therefore increases the penalty at Step 4 by way of an uplift of 200%. In so doing the Authority has paid regard to the following concerns:

a) The detriment and inconvenience to customers of Pritchard; and

b) Mr Gillespie's reckless behaviour contributed to the loss of £3 million of Pritchard's client money, including taking into account that he was the dominant force at Pritchard in introducing, characterising and negotiating the Offshore Facility.

c) His failure, on 7/8 February 2012, to advise Mr Welsby and initially the Authority that the funds were only conditionally available, and therefore could not qualify as client funds.

55. The Step 4 figure is therefore **£144,000**.

Serious financial hardship

56. Pursuant to DEPP 6.5D.2G, (text of guidance provided in Annex) the Authority will consider reducing the amount of a penalty if an individual will suffer serious financial hardship as a result of having to pay the entire penalty. The Authority accepts that the payment of a penalty of £100,800 would cause Mr Gillespie serious financial hardship. Mr Gillespie has provided verifiable evidence of serious financial hardship. The Authority has therefore reduced the penalty to **£15,100**.

Step 5: settlement discount

57. The Authority and Mr Gillespie reached agreement at Stage 1 and so a 30% discount applies to the Step 4 figure.

58. The Step 5 figure is therefore **£10,500**.

Proposed Penalty

59. The Authority therefore proposes to impose a total financial penalty of **£10,500**.

PROCEDURAL MATTERS

Decision maker

60. The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.

61. This Final Notice is given under, and in accordance with, section 390 of the Act.

Manner of and time for Payment

62. The financial penalty must be paid in three instalments as follows:

    a) £2,500 by 31 January 2015;

    b) £4,000 by 31 January 2016; and

    c) £4,000 by 31 January 2017.

63. The financial penalty must be paid in full by Mr Gillespie to the Authority by no later than 31 January 2017.

If the financial penalty is not paid

64. If all or any of the financial penalty is outstanding on 1 February 2017, the Authority may recover the outstanding amount as a debt owed by Mr Gillespie and due to the Authority.

Publicity

65. 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 Authority must publish such information about the matter to which this notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to you or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

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

Authority contacts

67. For more information concerning this matter generally, contact Paul Howick (direct line: 020 7066 7954 /email: paul.howick@fca.org.uk) of the Enforcement and Financial Crime Division of the Authority.

Megan Forbes

Financial Conduct Authority, Enforcement and Financial Crime Division

ANNEX

RELEVANT STATUTORY AND REGULATORY PROVISIONS

RELEVANT STATUTORY PROVISIONS

a. The Authority's statutory objectives, set out in section 1B(3) of the Act, include the consumer protection objective and the integrity objective.

Disciplinary Powers

b. Section 66 of the Act provides that the Authority may take action against a person if it appears to the Authority that he is guilty of misconduct and the Authority is satisfied that it is appropriate in all the circumstances to take action against him. A person is guilty of misconduct if, while an approved person, he has failed to comply with a statement of principle issued under section 64 of the Act, or has been knowingly concerned in a contravention by a relevant authorised person of a relevant requirement imposed on that authorised person.

Prohibition Order

c. Section 56 of the Act provides that the Authority may 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 Authority that that individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person, exempt person or a person to whom, as a result of Part 20, the general prohibition does not apply in relation to that activity. Such an order may relate to a specified regulated activity, any regulated activity falling within a specified description, or all regulated activities.

Imposition of financial penalty

d. Section 206(1) of the Act provides:

"If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act… it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate."

RELEVANT REGULATORY PROVISIONS

Statements of Principle and Code of Practice for Approved Persons

e. The Authority's Statements of Principle and Code of Practice for Approved Persons ("APER") have been issued under section 64 of the Act.

f. Statement of Principle 1 states:

"An approved person must act with integrity in carrying out his accountable functions."

g. The Code of Practice for Approved Persons sets out descriptions of conduct which, in the opinion of the Authority, do not comply with a Statement of Principle. It also sets out factors which, in the Authority's opinion, are to be taken into account in determining whether an approved person's conduct complies with a Statement of Principle.

The Fit and Proper Test for Approved Persons

h. The part of the Authority's Handbook entitled "The Fit and Proper Test for Approved Persons" ("FIT") sets out the criteria that the Authority 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.

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

The Enforcement Guide

j. The Enforcement Guide ("EG") sets out the Authority's approach to exercising its main enforcement powers under the Act.

k. Chapter 7 of the EG sets out the Authority's approach to exercising its power to impose a financial penalty.

l. Chapter 9 of EG sets out the Authority's policy in relation to prohibition orders.

m. EG 9.1 states that the Authority may exercise this power where it considers that, to achieve any of its regulatory objectives, it is appropriate either to prevent an

individual from performing any functions in relation to regulated activities or to restrict the functions which he may perform.

DEPP

n. Chapter 6 of DEPP sets out the Authority's statement of policy with respect to the imposition and amount of financial penalties under the Act.

o. DEPP 6.5D.2G states that:

(1) In assessing whether a penalty would cause an individual serious financial hardship, the FCA will consider the individual's ability to pay the penalty over a reasonable period (normally no greater than three years). The FCA's starting point is that an individual will suffer serious financial hardship only if during that period his net annual income will fall below £14,000 and his capital will fall below £16,000 as a result of payment of the penalty. Unless the FCA believes that both the individual's income and capital will fall below these respective thresholds as a result of payment of the penalty, the FCA is unlikely to be satisfied that the penalty will result in serious financial hardship.

(2) The FCA will consider all relevant circumstances in determining whether the income and capital threshold levels should be increased in a particular case.

(3) The FCA will consider agreeing to payment of the penalty by instalments where the individual requires time to realise his assets, for example by waiting for payment of a salary or by selling property.

(4) For the purposes of considering whether an individual will suffer serious financial hardship, the FCA will consider as capital anything that could provide the individual with a source of income, including savings, property (including personal possessions), investments and land. The FCA will normally consider as capital the equity that an individual has in the home in which he lives, but will consider any representations by the individual about this; for example, as to the exceptionally severe impact a sale of the property might have upon other occupants of the property or the impracticability of re-mortgaging or selling the property within a reasonable period.

(5) The FCA may also consider the extent to which the individual has access to other means of financial support in determining whether he is able to pay the penalty without being caused serious financial hardship.

(6) Where a penalty is reduced it will be reduced to an amount which the individual can pay without going below the threshold levels that apply in that case. If an individual has no income, any reduction in the penalty will be to an amount that the individual can pay without going below the capital threshold.

(7) There may be cases where, even though the individual has satisfied the FCA that payment of the financial penalty would cause him serious financial hardship, the FCA considers the breach to be so serious that it is not appropriate to reduce the penalty. The FCA will consider all the circumstances of the case in determining whether this course of action is appropriate, including whether:

(a) the individual directly derived a financial benefit from the breach and, if so, the extent of that financial benefit;(b) the individual acted fraudulently or dishonestly with a view to personal gain;

(c) previous FCA action in respect of similar breaches has failed to improve industry standards; or

(d) the individual has spent money or dissipated assets in anticipation of FCA or other enforcement action with a view to frustrating or limiting the impact of action taken by the FCA or other authorities.

Client Money Rules

p. The Client Assets section of the Authority's Handbook ("CASS") sets out the requirements relating to holding client assets and client money.

q. Set out below are relevant extracts from CASS 7.4 and 7.6:

CASS 7.4.1

"A firm, on receiving any client money, must promptly place this money into one or more accounts opened with any of the following:

(1) a central bank;

(2) a CRD credit institution;

(3) a bank authorised in a third country;

(4) a qualifying money market fund."

CASS 7.6.1

“A firm must keep such records and accounts as are necessary to enable it, at any time and without delay, to distinguish client money held for one client from client money held for any other client, and from its own money.”

CASS 7.6.2

“A firm must maintain its records and accounts in a way that ensures their accuracy, and in particular their correspondence to the client money held for clients.”

CASS 7.6.5

“A firm should ensure that it makes proper records, sufficient to show and explain the firm's transactions and commitments in respect of its client money.”

CASS 7.6.6

“(1) Carrying out internal reconciliations of records and accounts of the entitlement of each client for whom the firm holds client money with the records and accounts of the client money the firm holds in client bank accounts and client transaction accounts should be one of the steps a firm takes to satisfy its obligations under CASS 7.6.2 R, and where relevant SYSC 4.1.1 R and SYSC 6.1.1 R.

(2) A firm should perform such internal reconciliations:

(a) as often as is necessary; and

(b) as soon as reasonably practicable after the date to which the reconciliation relates;

to ensure the accuracy of the firm's records and accounts.

(3) The standard method of internal client money reconciliation sets out a method of reconciliation of client money balances that the FCA believes should be one of the steps that a firm takes when carrying out internal reconciliations of client money.”

CASS 7.6.10

“(1) A firm should perform the required reconciliation of client money balances with external records:

(a) as regularly as is necessary; and

(b) as soon as reasonably practicable after the date to which the reconciliation relates;

to ensure the accuracy of its internal accounts and records against those of third parties by whom client money is held.

(2) In determining whether the frequency is adequate, the firm should consider the risks which the business is exposed, such as the nature, volume and complexity of the business, and where and with whom the client money is held."

CASS 7.6.13

"When any discrepancy arises as a result of a firm's internal reconciliations, the firm must identify the reason for the discrepancy and ensure that:

(1) any shortfall is paid into a client bank account by the close of business on the day that the reconciliation is performed; or

(2) any excess is withdrawn within the same time period (but see CASS 7.4.20 G and CASS 7.4.21 R)."

CASS 7.6.16

"A firm must inform the FCA in writing without delay:

(1) if it has not complied with, or is unable, in any material respect, to comply with the requirements in CASS 7.6.1 R, CASS 7.6.2 R or CASS 7.6.9 R;

(2) if having carried out a reconciliation it has not complied with, or is unable, in any material respect, to comply with CASS 7.6.13 R to CASS 7.6.15 R."