# FINAL NOTICE

To: **Energy Finance (UK) Limited**

Of: **41 Stevens House**
**Jerome Place**
**Kingston Upon Thames**
**KT1 1HX**

Date: 23 August 2004

**TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("the FSA") proposes to take the following action**

## 1. ACTION

1.1 By an application received by the FSA on 22 July 2003 ("the Application") Energy Finance (UK) Limited ("Energy Finance") has applied under section 44 of the Financial Services and Markets Act 2000 ("the Act") to vary its Part IV permission to remove the requirement that "Independent Compliance Reviews are to be undertaken on a quarterly basis".

1.2 For the reasons listed below and pursuant to section 52(7) of the Act, the FSA has refused the Application.

## 2. REASONS FOR THE ACTION

### Summary

2.1 By its Decision Notice ("the Decision Notice") dated 22 July 2004 the FSA informed of its decision to refuse the firm's application and the firm was given the opportunity to make representations to the FSA about that action.

2.2 As no representations have been received by the FSA from the firm within the time allowed by the Decision Notice, the default procedures (see DEC 4.4.13 of the Decision Making Manual) permit the conclusions described in the Decision Notice to be regarded as undisputed.

2.3 On the basis of the facts and matters described below, the FSA has concluded that it cannot ensure that Energy Finance will satisfy, and continue to satisfy, the threshold conditions set out in Schedule 6 to the Act ("the threshold conditions") as, in the opinion of the FSA, Energy Finance has not satisfied the FSA that it has adequate resources in relation to its regulated activities and that it would be ready, willing and organised to comply on a continuing basis with the requirements and standards under the regulatory system which will apply to the firm without the requirement (threshold conditions 4 and 5)

### Relevant Statutory Provisions

2.4 Section 41(2) of the Act requires the FSA, in varying a Part IV permission, to ensure that the person concerned will satisfy, and continue to satisfy, the threshold conditions in relation to all of the regulated activities for which he has or will have permission.

### Relevant Guidance

2.5 In exercising its powers in relation to the variation of a Part IV permission, the FSA must have regard to guidance published in the FSA Handbook. The main considerations in relation to the action specified are set out below.

***Threshold condition 4: Adequate Resources***

2.6 COND 1.3.2G states that, in relation to threshold conditions 4 and 5, the FSA will consider whether a firm is ready, willing and organised to comply on a continuing basis with the requirements and standards under the regulatory system which will apply to the firm if the variation of its Part IV permission is granted.

2.7 COND 2.4.2G states that threshold condition 4 requires the FSA to ensure that a firm has adequate resources in relation to the specific regulated activity which it seeks to carry on. In this context, the FSA will interpret the term “adequate” as meaning sufficient in terms of quantity, quality and availability, and “resources” as including all financial resources, non financial resources and means of managing its resources.

***Threshold condition 5: Suitability***

2.8 COND 2.5.2G(1) states that threshold condition 5 requires the firm to satisfy the FSA that it is “fit and proper” to have its Part IV permission varied having regard to all the circumstances, including the range and nature of its proposed regulated activities and the overall need to be satisfied that its affairs are and will be conducted soundly and prudently.

2.9 COND 2.5.2G(2) states that the FSA will also take into consideration anything that could influence a firm’s continuing ability to satisfy threshold condition 5.

2.10 COND 2.5.4G allows the FSA to have regard to all relevant matters, including whether the firm:

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

(b) will have a competent and prudent management; and

(c) can demonstrate that it will conduct its affairs with the exercise of due skill, care and diligence.

***Integrity and compliance with proper standards***

2.11 COND 2.5.6G allows the FSA, in determining whether a firm will satisfy, and continue to satisfy, threshold condition 5 in respect of conducting its business with integrity and in compliance with proper standards, to have regard to relevant matters including whether:

- the firm is ready, willing and organised to comply with the requirements and standards under the regulatory system (COND 2.5.6G(1));
- the firm has taken reasonable care to establish and maintain effective systems and controls for the compliance with applicable requirements and standards under the regulatory system that will apply to the firm (COND 2.5.6G(6));
- the firm has put in place procedures which are reasonably designed to:

  (a) ensure that it has made its employees aware of and compliant with those requirements and standards under the regulatory system that apply to the firm and the regulated activities for which it has permission;

  (b) ensure that its approved persons are aware of those requirements and standards under the regulatory system applicable to them;

  (c) determine that its employees are acting in a way compatible with the firm adhering to those requirements and standards; and

  (d) determine that its approved persons are adhering to those requirements and standards (COND 2.5.6G(7)).

***Competent and prudent management***

2.12 COND 2.5.7G permits the FSA, in determining whether a firm will satisfy and continue to satisfy threshold condition 5 in respect of having competent and prudent management and exercising due skill, care and diligence, to have regard to relevant matters including whether:

- the governing body of the firm is made up of individuals with an appropriate range of skills and experience to understand, operate and manage the firm's regulated activities (COND 2.5.7G(1));
- the governing body of the firm is organised in such a way that enables it to address and control the regulated activities of the firm (COND 2.5.7G(3));
- the firm has made arrangements to put in place an adequate system of internal control to comply with the requirements and standards under the regulatory system (COND 2.5.7G(5));

- the firm has conducted enquiries that are sufficient to give it reasonable assurance that it will not be posing unacceptable risks to consumers or the financial system (COND 2.5.7G(9)).

**Facts and Matters Relied Upon**

***Background***

2.13 Energy Finance submitted an Application to vary its Part IV permission on 22 July 2003 to remove the requirement that "independent compliance reviews are to be undertaken on a quarterly basis".

2.14 At the time of the application Energy Finance was a limited company with 2 directors, Danesh Varma and Jayanta Mitra and one adviser. It now has 6 approved persons, of whom the 2 directors are CF1 and CF3s, 3 are Investment Advisers CF21s and the sixth is CF10 and CF11 (although he is also approved with another regulated firm as CF1, 8, 10, 11, 13 and 27).

2.15 Energy Finance was authorised in 1995 by IMRO with the intention of marketing and acting as General Partner to limited partnerships investing in oil and gas opportunities. During IMRO's periodic visit on 12 December 1997 it informed IMRO that it had had its last sale in the financial year ending 30 June 1997 and had ceased conducting investment business. Following this visit IMRO concluded that compliance monitoring had not been undertaken and removed all categories of Permitted Business from its permission on 6 March 1998.

2.16 On 9 December 1999 the firm applied for the following categories of Permitted Business which were granted on 6 January 2000:

- G3 – Arranging deals in investments; and
- G12 – Marketing Unregulated Collective Investment Schemes.

2.17 In addition to the above permissions, a Limitation and another Special Condition, which substituted the Special Condition of 1998, were also added. They read as :

- Limitation - "the activities were limited to the TIP Trust Bermuda and are only in respect of Non-Private Customers".
- Special Condition - "Independent Compliance Reviews are to be undertaken on a quarterly basis".

2.18 On 2 May 2001 IMRO conducted another periodic Supervision visit to Energy Finance, reviewing their Systems & Controls, Compliance Procedures and documentation (sample). IMRO told Energy Finance that it must have an immediate independent compliance visit. CCL did so in July 2001. Energy Finance have confirmed that this was their last review as the firm has been dormant since 1997.

2.19 CCL made a number of recommendations that have not been acted upon (see below). It also found a number of compliance failings as follows:

(a) Personal Account Dealing (PAD)

These had been lost by the firm as recorded in the IMRO 2001 Visit Report. The firm's Compliance Officer confirmed that no PAD was undertaken. CCL found no evidence that any PAD was undertaken in the period. CCL provided the firm with a PAD replacement in July 2001.

(b) Gifts and Benefits Register (G&B)

These had also been lost by the firm as recorded in the IMRO 2001 Visit Report. CCL noted that the CEO did not undertake any review of G&B given or received since the firm's authorisation. CCL repeated their recommendation regarding the reviews of G&B on a quarterly basis and evidencing it by signing them off. CCL provided the firm with a G&B replacement register in July 2001.

(c) Investment Advertisements

This register had also been lost as was recorded in the IMRO 2001 Visit Report. Although no advertisements were issued or approved, CCL recommended keeping the register up-to-date. CCL provided the firm with a replacement register in July 2001.

(d) IMRO Rule Breaches

The firm did not record its failure to appoint a Finance Officer, nor to carry out checks on its Financial Resources position, nor to submit its Quarterly Financial Returns for years 2000 and 2001 on time.

(e) Financial Resources and Financial Returns ("FR")

CCL had recommended in November 2000 that the firm should have a FR file and prepare monthly FR statements to demonstrate their compliance with FRR. These were not done and were not recorded in the Breach Register.

(f) Accounting and Financial Control Systems

CCL had recommended in November 2000 that the firm should instruct its auditors/accountants to document its accounting and financial control systems and procedures. These were not done and were not recorded in the Breach Register.

2.20 In July 2003 the firm applied for the removal of the requirement for independent compliance reviews to be undertaken on a quarterly basis since it has been dormant since 1997 and one of its Directors has subsequently explained it is not able to afford independent compliance reviews. The firm has also appointed a Compliance Officer who is familiar with the firm's business and will spend one day a quarter towards his compliance monitoring duties with the firm. The remainder of the time the firm will rely on self-compliance.

2.21 The FSA is not of the view that this will be adequate because:

(a) Prospective Level of Business

Although the firm justifies the decrease in the compliance function on the basis of its limited scope of regulated activities, the firm's level of business is not restricted. The firm's Business Plan (see below) is based on the firm arranging two units in TIP Trust Bermuda valued at $150,000 each, resulting in the firm's income of £3,000 for 2004. The firm has employed three CF21 Investment Advisers (two of which also have CF27 Investment Management) to provide this level of income as well as to plan for additional products. At the later stage of processing this application (i.e. 6 January 2004) the firm has stated its plans to add further two off-shore funds once the compliance costs become affordable by the approval of this variation.

(b) Type of Business

Although the firm's regulated activities are restricted to transaction-only activities (promoting and arranging) in respect of the TIP Trust Bermuda and Intermediate and

Market Counterparty Customers only, there are concerns regarding the adequacy of day-to-day monitoring of such activities by individuals with diverse involvements and responsibilities elsewhere (see (c) below).

(c) The variety of places at which the firm's Employees work

The firm's Director and its employees are also employed by and authorised with two other FSA authorised firms (Innvotec Ltd and Enterprise Private Capital Ltd). Diversity of these firms' locations (London and Peterborough) and their business types (non-ISD Venture Capital Company and ISD Discretionary Investment Managers) as well as the authorised individuals' involvement within these firms ranging from Senior Management Control Functions to Customer Control Functions, would require experienced compliance staff to ensure a focused approach to day-to-day compliance monitoring of the firm's activities.

(d) The conceptual difference between a Independent Compliance Review and internal compliance monitoring.

In making its proposal that their Compliance Officer would spend only one day a quarter on his compliance monitoring duties, the firm has failed to understand that:

i. The role of the external compliance consultants was to provide quarterly reviews and not to monitor the firm's activities and its advisers which should be done on a day-by-day basis.

ii. The external review was to be done by a firm specialising in this field which enabled it to review the firm's activities in a day. Their task was further eased by the fact that at the time the firm was not trading and had no Investment Advisers.

iii. The "one-day arrangement" is in breach of the firm's Compliance Procedures Manual. This states that the Compliance Officer has responsibility for monitoring the firm's staff on a day-to-day basis (Section 4.6 Compliance Oversight Function, volume 1) and is responsible for preparing Compliance Monitoring Programmes on a monthly as well as weekly basis (Personal Account Dealing, volume 3).

(e) The firm has not acted on the recommendations of CCL's Quarterly Compliance Review of July 2001.

i. Internal Compliance Monitoring

1. The firm did not undertake internal compliance monitoring test 19 "Financial Resources" (FR). The firm's then compliance officer said that the firm would begin producing monthly FR statements to allow them to undertake the monthly FR test in the near future. The firm has not done so.

2. The compliance monitoring work was not accompanied by (or referenced to) evidence of the work done to provide an audit trail. CCL recommended reviewing this practice. The firm has not done so.

3. CCL noted that the firm held two Board Meetings in January and April 2001 and compliance matters were discussed. CCL recommended strengthening the reporting of compliance matters, i.e. the agenda for

each board meeting should include compliance matters, and the Compliance Officer provide his reports. The firm has not done so.

ii. Customer Categorisation

1. The firm has not implemented the CCL recommendation regarding the justification behind the firm's non-private categorisation of its customer, TIP (Bermuda) Ltd.

2. There is no evidence of customer categorisation to whom the Fund would be marketed.

2.22 The FSA is also of the view that the firm is not suitable to conduct its own compliance program because the firm's procedures and arrangements have not been adjusted for the firm's proposed business:

(a) The firm provided a draft of their Compliance Procedures Manual in April 2004. Although this Manual is identical to that of Enterprise Private Capital Limited, the firm's approach to internal compliance does not correspond with the firm's written procedures.

(b) The firm has appointed the Compliance Officer who has full-time duties and obligations of a Managing Director and a Compliance Officer with another FSA authorised firm and accepts that he can only contribute limited time (one day a quarter) and efforts towards his compliance monitoring duties with the firm.

(c) The firm does not understand the importance of the robust compliance arrangements in place for monitoring the firm's 3 newly appointed Investment Advisers since it is unclear how they will be monitored.

(d) The firm has been constantly late with their Annual Financial Returns and Audited Accounts submitted to the FSA. The firm has not yet submitted their completed 2003 Auditors Report to FSA.

(e) The firm's business plan is vague on the firm's proposed activities as well as on their timescale. This is a contrast to the firm's previous business plan provided to IMRO as part of the firm's application to vary their permission in December 1999. The firm was assisted in this application by CCL. Although the plan was clear as to the firm's proposed business it was never implemented by the firm.

## 3. CONCLUSIONS

On the basis of the facts and matters described above, the FSA has concluded that these failings are material and that it therefore cannot satisfy the requirement of section 41(2) of the Act that it must ensure that Energy Finance will satisfy, and will continue to satisfy, the threshold conditions in relation to all of the regulated activities for which Energy Finance would have permission if the Application was granted.

## 4. DECISION MAKER

The decision which gave rise to the obligation to give this Final Notice was made by Michael Lord, Head of Department, Small Businesses.

## 5. IMPORTANT NOTICES

This Final Notice is given to you under section 390(1) of the Act. (See DEC 2.3 of the Decision Making Manual)

### Confidentiality and publicity

Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which a Final Notice relates. Under those provisions, the FSA must publish such information about the matter to which this Final Notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to you or prejudicial to the interests of consumers.

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