
FINAL NOTICE

To: **Richard Bernard Charles** **Scotts Private Client Services Limited**

Of: **Chyfields** **3 Rubislaw Terrace**
 Flexford Road **Aberdeen**
 Normandy **AB10 1XE**
 Surrey GU3 3EE

Date: **18 May 2004**

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

ACTION

1. The FSA gave you a decision notice dated 24 March 2004 which notified you, Richard Bernard Charles, that pursuant to Section 63 of the Financial Services and Markets Act ("FSMA"), the FSA had decided to withdraw the approval granted to you to perform the controlled function of investment adviser for Scotts Private Client Services Limited ("Scotts").
2. Neither you nor Scotts as an interested party have referred the matter to the Financial Services and Markets Tribunal within 28 days of the date on which the decision notice was given to you. Accordingly, for the reasons set out below, the FSA now hereby withdraws the approval granted to you to perform controlled function 21: Investment adviser for Scotts. This action has effect from 20 May 2004.

REASONS FOR ACTION

Introduction

3. The FSA considers that Richard Bernard Charles ("Mr Charles") is not fit and proper to perform the function to which his approval relates. This action arises from the fact that Mr Charles induced investors to participate in a US dollar offshore investment scheme ("the scheme") by falsely representing that the funds placed in the scheme

benefited from a US dollar currency hedge to minimise exchange-rate risk and that he concealed material information from his employers in relation to the US dollar currency hedge. In the FSA's view this conduct demonstrates a lack of both honesty and integrity and of competence and capability.

Relevant statutory provisions

4. The FSA is authorised by FSMA to exercise the powers contained in Section 63 of FSMA, which include the following:

- "(1) [the FSA] may withdraw an approval given under Section 59 if it considers that the person in respect of who it was given is not a fit and proper person to perform the function to which the approval relates.*
- (2) When considering whether to withdraw its approval, [the FSA] may take into account any matter which it could take into account if it were considering an application made under section 60 in respect of performance of the function to which the approval relates".*

Relevant guidance

5. In exercising its powers in relation to the withdrawal of an approval the FSA has had regard to the guidance published in the FSA handbook. The FSA's Enforcement manual ("ENF") contains guidance, at ENF 7, as to the criteria which the FSA will consider when exercising its power to withdraw approval.
6. ENF 7.5.1 states that the FSA may withdraw its approval only if it considers that the person in respect of whom it was given is not a fit and proper person to perform the function to which the approval relates.
7. ENF 7.5.2 further states that the FSA recognises that its decision to withdraw approval will often have a substantial impact on those concerned. When it considers whether to withdraw approval from a person it will take account of all relevant factors, including, but not limited to:

- "(2) the criteria for assessing the fitness and propriety of approved persons. These are contained in [the fit and proper test in the FSA handbook] FIT 2.1 (Honesty, integrity and reputation); FIT 2.2 (Competence and Capability). The criteria include:*
 - (a) Honesty, integrity and reputation; this includes an individual's openness and honesty in dealing with consumers, market participants and regulators, and the ability and willingness to comply with requirements placed on him by or under FSMA as well as with other legal and professional obligations and ethical standards;*
 - (b) Competence and capability; this includes having necessary skills to carry out the controlled function that he is performing.*
- (3) whether, and to what extent, the approved person hasfailed to comply with the Statements of Principle*;

- (4) *the relevance, materiality and length of time since the occurrence of any matters indicating unfitness;*
 - (5) *the severity of risk which a person poses to consumers and confidence in the financial system;*
 - (6) *the previous disciplinary record and general compliance history of the person including whether the FSA (or any previous regulator) has previously imposed a disciplinary sanction on the person."*
8. ENF 7.5.4 states that the FSA may also take account of the particular controlled function which an approved person is carrying out within a firm, the nature of the activities of the firm concerned and the markets within which it operates.
 9. The Statements of Principle and Code of Practice for Approved Persons ("APER") in the FSA handbook issued under subsections (1) and (2) of Section 64 of FSMA apply to approved persons exercising a controlled function.
 10. Statement of Principle 1 requires that "*an approved person must act with integrity in carrying out his controlled function*". Deliberately misleading (or attempting to mislead) by act or omission a client or his firm or the FSA falls within the Principle. Such behaviour includes misleading a client about the risks of an investment and providing false or inaccurate documentation or information.
 11. Statement of Principle 2 requires that "*an approved person must act with due skill, care and diligence in carrying out his controlled function*". Failing to inform a customer or his firm of material information in circumstances where he was aware, or ought to have been aware, of such information, and of the fact that he should provide it falls within this Principle.

Facts and matters relied on:

Background

12. Scotts is an accountancy firm regulated by the Institute of Chartered Accountants of Scotland ("ICAS"). However, since 1 December 2001 for the purpose of investment business Scotts has been an authorised person and regulated by the FSA under FSMA.
13. Scotts operates from three offices: Aberdeen, Edinburgh and London. The Aberdeen and London offices are concerned with the provision of tax advice which is Scotts' core business. The Aberdeen office was, during the relevant period, staffed by Scotts' directors. At the material time therefore Scotts' management was based in Aberdeen.
14. Mr Charles has been employed since May 2001 by Scotts at its London office with the title of Associate Director. Since 17 September 2002 he has been approved to perform the controlled function of investment adviser for Scotts.
15. Prior to joining Scotts, Mr Charles had worked in the insurance and financial services industry for a number of employers. He was a Registered Individual with the then Securities and Futures Authority between 20 November 2000 and 1 June 2001.

16. In 2001 Mr Charles was offered employment by Scotts to help establish its new London office, where Scotts wished to promote tax driven investment schemes. The FSA understands that it was intended that Mr Charles would use his contacts with independent financial advisers to promote and develop Scotts' products.
17. In the period 2001-2002 Scotts introduced investors to the scheme operated by a third party whereby investors were ostensibly offered high returns at low risk. The majority of investors had in turn been introduced to Scotts by intermediaries who were authorised persons.
18. Mr Charles invested US \$70,141 of his own funds in the scheme in November 2001.

Commission

19. Scotts estimated that the funds in the scheme would achieve a high return at low risk. A schedule from the third party operator received in March 2002 indicated a return of 28% per annum. If interest received on monies invested in the Scheme exceeded 15% per annum, then anything over the 15% was to be retained by Scotts and split in accordance with a formula that was agreed by Scotts' management. Although there was no guarantee given to Scotts' employees that the funds would earn 15% interest, the expectation was that the return would be higher than 15%. Mr Charles' allocation of commission was 20% of the total commission earned on the London clients.
20. The actual sum allocated to Mr Charles as a result of introducing clients' funds to the scheme was US \$35,149. This was rolled up and retained within the scheme to earn further interest.

The US Dollar Currency Hedge

21. Another authorised person asked Scotts to prepare an explanatory document about the scheme for its clients. On 11 October 2001 the first draft was prepared by another Scotts' employee and sent to Mr Charles and Scotts' management for comment. This document was Scotts' understanding of the scheme. In the section headed "*What are the risks?*" a US\$ / £ foreign exchange risk was identified.
22. In or about December 2001 the other authorised person who had requested the explanatory document enquired of Mr Charles whether funds paid into the scheme by investors introduced by that authorised person might be protected by a currency hedge to reduce its risk. Mr Charles understood that this was a condition of their participation in the scheme.
23. Mr Charles knew that Scotts' management had given an instruction that a US dollar currency hedge should not be offered but has stated that he understood that to mean that Scotts should not bear the costs of arranging it. Therefore, when he believed that he had identified a method of hedging without cost to Scotts he proceeded to offer a US dollar currency hedge to investors introduced by this other authorised person. Mr Charles understood that this method allowed funds paid into the scheme to be hedged retrospectively at the exchange rate applying at the date of investment. Mr Charles did not discuss or agree this hedging method with Scotts' management.

24. In these circumstances and without the knowledge of Scotts' management, Mr Charles purported to offer a US dollar currency hedge to investors introduced by the other authorised person without having first put the hedge in place. As a consequence between 18 January 2002 and 5 August 2002 US \$4.2 million was transferred by 20 investors to Scotts for investment in the scheme in the belief that the monies were subject to a US dollar currency hedge.
25. In due course periodic statements produced by Mr Charles were sent to the 20 investors to the effect that there was in place a currency hedge stating that "*the initial cash deposit is hedged at a charge of 1% pa at the exchange of...*". In fact, at no time was there a US dollar currency hedge in place.
26. In June and July 2002 four of the individuals who believed their funds were hedged requested Scotts to withdraw funds from the scheme. In total these withdrawals amounted to approximately 5% of the total funds placed through Mr Charles by investors who believed that their funds were hedged. Due to exchange-rate movements since the date of their investment and in the absence of a US dollar currency hedge there was a shortfall of £9,000 in the sums to be repaid from the scheme. This shortfall was funded by Mr Charles personally, less the purported 1% administration charge noted on the above-mentioned periodic statements. The fact that Mr Charles paid these sums personally was not communicated to the four individuals or to Scotts' management.
27. The authorised person which had introduced these investors to the scheme was informed by Mr Charles in an email dated 22 July 2002 that a currency hedge would not be available on any further sums invested. However, Mr Charles incorrectly stated that existing funds continued to benefit from a US dollar currency hedge, which he knew to be untrue. Scotts' management was unaware of these statements made on behalf of the firm.
28. It was not until November 2002, and after the FSA took action to end the scheme, that Mr Charles informed the other authorised person and Scotts' management of the full details of the hedge and that the funds had never been hedged.

Issue 1 - Honestly, integrity and reputation

29. The FSA considers that Mr Charles' conduct is inconsistent with the requirements of honestly, integrity and reputation contained in the Fit and Proper Test for approved persons in the FSA handbook. This is for the following reasons:
 - Mr Charles made untruthful representations to an authorised person that money invested in the scheme benefited from the protection of a US dollar currency hedge on which investors relied, including as follows:
 - the production and dissemination of client statements with a footnote falsely stating that: "*the initial cash deposit is hedged at a charge of 1% pa at the exchange rate of...*";
 - Mr Charles' email of 22 July 2002 falsely advising the authorised person that: "*As a result of the large movement in [the] exchange rate...we are unable to take further sums on which a hedge is required. This does not affect monies already held only any further funds*";

- While Mr Charles has asserted that it was not until June or July 2002 that he discovered that a US dollar currency hedge could not be effected in respect of monies already invested, he failed then to take any steps to correct the false representations already made to the other authorised person and investors.
 - Mr Charles' intended to retain for his own benefit the amount of the administration charge of 1 percent even though there was no US dollar currency hedge;
 - Mr Charles stood to benefit from commission for every sum invested in the scheme and only informed the other authorised person and his employers of the true position when forced by circumstances to do so in November 2002.
30. In the view of the FSA, Mr Charles was not candid and truthful in all his dealings with the other authorised person, investors and his employer and also failed to demonstrate a readiness and willingness to comply with the requirements and standards of the regulatory system and with other legal, regulatory and professional requirements and standards.
31. The FSA also considers that Mr Charles' conduct since 17 September 2002 when he became an approved person has contravened Statement of Principle 1 which requires an approved person to act with integrity in carrying out his controlled function.

Issue 2 - Competence and capability

32. Mr Charles has informed the FSA that, initially, he believed that funds invested in the scheme might retrospectively be made subject to a US dollar currency hedge and only later discovered this was not possible. The FSA considers that Mr Charles' belief that a US dollar currency hedge might be put in place retrospectively demonstrates a fundamental misunderstanding of the nature and working of such instruments. Mr Charles should have ensured that he had the appropriate competence and capability before offering a hedge.
33. The FSA considers that in this respect Mr Charles' conduct also failed to meet the requirements of competence and capability contained in the Fit and Proper Test for approved persons in the FSA handbook.
34. The FSA further considers that in this respect Mr Charles' conduct since 17 September 2002 when he became an approved person has contravened Statement of Principle 2 which requires an approved person to act with due skill, care and diligence in carrying out his controlled function.

Conclusion

35. The FSA has concluded that Mr Charles' actions in relation to the US dollar currency hedge, including his deception both of investors and his employer, demonstrate that he is not a fit and proper person to perform the controlled function of investment adviser for Scotts and the FSA hereby withdraws his approval accordingly.

IMPORTANT

36. This Final Notice is sent to you in accordance with Section 390 of FSMA.

Publicity

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

Interested party

39. The FSA gave a copy of the Decision Notice to Scotts as an interested party pursuant to Section 63(4) of FSMA. Accordingly, the FSA must also give a copy of this notice to Scotts.

FSA contacts

40. For more information concerning this matter generally, please contact John Tutt or Richard Powell at the FSA (direct lines: 020 7066 1240 and 020 7066 0528).

Julia M R Dunn
Head of Retail Selling
FSA Enforcement Division