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**FINAL NOTICE**

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To: **Mr John Christopher Hughes**

Individual Reference Number: **JCH01190**

29 April 2014

**1. ACTION**

- 1.1. For the reasons given in this notice, the Authority hereby makes an order prohibiting John Christopher Hughes from performing any function in relation to any regulated activities carried on by any authorised or exempt persons, or exempt professional firm. This order takes effect from 29 April 2014.
- 1.2. Mr Hughes cooperated with the Authority during the course of its investigation and agreed to settle at an early stage.

**2. SUMMARY OF REASONS**

- 2.1. During the period 1 January 2011 and 14 September 2011 (the "Relevant Period") Mr Hughes worked in the Global Synthetic Equities division of the London branch of the investment bank of UBS AG (the "Firm"). He was the most senior trader on the Exchange Traded Funds Desk (the "Desk").
- 2.2. During the Relevant Period, Kweku Mawuli Adoboli, another trader on the Desk, undertook unauthorised trading which caused losses amounting to \$2.3 billion. Part of the unauthorised trading involved creating and using an undeclared fund of profits, termed the "Umbrella", which had the effect of manipulating the Desk's reported profit and loss.

- 2.3. During the Relevant Period, Mr Hughes was aware of the existence of the Umbrella and that it was being used to misrepresent the Desk's profit and loss. In addition he made enquiries about the Umbrella's size and influenced decisions about how it would be funded and used.
- 2.4. Mr Hughes did not consider the Umbrella to be honest and knew that the Firm would not have authorised its use. Mr Hughes' conduct in relation to the Umbrella was dishonest and demonstrates that he is not a fit and proper person to perform functions in relation to any regulated activity carried on by an authorised or exempt person.
- 2.5. One of the FCA's statutory objectives is to protect and enhance the integrity of the UK financial system. One of the ways in which the FCA seeks to achieve this objective is by keeping dishonest individuals out of the financial services industry.
- 2.6. The Authority therefore makes a full prohibition order pursuant to section 56 of the Financial Services and Markets Act 2000 (the "Act") prohibiting John Christopher Hughes from performing any function in relation to any regulated activities carried on by any authorised or exempt persons, or exempt professional firm.

### **3. DEFINITIONS**

The definitions below are used in this Decision 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

"the Desk" means the Exchange Traded Funds Desk in the Global Synthetic Equities Division of UBS AG

"the Firm" means UBS AG

"the Relevant Period" means the period between 1 January 2011 and 14 September 2011

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

"the Umbrella" means the undeclared fund of profits created by Mr Adoboli

#### 4. FACTS AND MATTERS

##### Mr Hughes' role

- 4.1. During the Relevant Period, Mr Hughes was employed as a trader on the Desk at the London branch of the Firm's Investment Bank. The Firm is a major global financial group with its headquarters in Zurich. Mr Hughes joined the Firm in September 2005 and moved to the Desk in October 2006.
- 4.2. Throughout the Relevant Period Mr Hughes worked on the Desk with Mr Adoboli and two junior traders. Mr Hughes was the most senior trader on the desk. He usually reported the Desk's daily profit and loss at the end of each trading day.
- 4.3. Mr Hughes was suspended by the Firm shortly after the arrest of Mr Adoboli. On 27 October 2011 Mr Hughes attended a disciplinary hearing at the Firm. On 31 January 2012 the Firm informed Mr Hughes of its decision to dismiss him for gross misconduct. He did not contest his dismissal.

##### The Umbrella

- 4.4. During the Relevant Period, and as Mr Hughes was aware, Mr Adoboli created and used a fund of profits which he termed the "Umbrella". The Umbrella was not declared to the Firm and worked in such a way that Mr Adoboli could choose when to release profit into the Desk's reported profit and loss. As a result it was possible to manipulate when profit or losses were shown.
- 4.5. Mr Hughes understood the funds in the Umbrella had accrued as a result of Mr Adoboli not declaring the entirety of profits he had made on his trades. Mr Hughes described his understanding of the Umbrella in the following way:

*"It was some profit that he [Mr Adoboli] hadn't declared that he was going to use when we had bad days on the book, because the way the book was structured, the previous year we'd dropped a lot of money to dividends and just copped actions on the book that you miss and they get checked differently to how you thought they were going to be treated and, you know, he just – he originally set it up so that we didn't have to – we didn't have that."*

Mr Hughes' involvement

- 4.6. Mr Hughes received written notification of the Umbrella's existence in a chat message with Mr Adoboli on 20 January 2011. On first finding out about the Umbrella, Mr Hughes understood that it represented profit that Mr Adoboli had not booked. He also understood that Mr Adoboli had a method of trading and settling a trade without declaring the profit or loss on that trade.
- 4.7. Mr Hughes stated that his initial reaction on learning of the Umbrella was that he felt "*a bit sick*". However by 7 February 2011, Mr Hughes had become supportive of the idea, stating to Mr Adoboli in a chat conversation that the Desk's year to date profit and loss should not include profits from the Umbrella.
- 4.8. Mr Hughes believed that nobody above him with responsibility for management of the Desk knew about the Umbrella or encouraged its use. Mr Hughes stated that, by not reporting the Umbrella when discussing the Desk's profit and loss with management, he was "*lying every day*".
- 4.9. During the Relevant Period, Mr Hughes knew the Umbrella was wrong, believed that he and Mr Adoboli should not have been using it and thought that if the Firm became aware of the Umbrella they would have lost their jobs. However he was not prepared to take the necessary steps to discontinue the Umbrella by reporting the matter to management.
- 4.10. Throughout the Relevant Period Mr Hughes made repeated enquiries into the size of the Umbrella. By way of example:
- (a) on 21 January 2011, (the day after the first recorded discussion of the Umbrella) Mr Hughes enquired of Mr Adoboli how much the Umbrella was worth. Mr Adoboli replied giving Mr Hughes a figure;
  - (b) on 11 February 2011 Mr Hughes enquired about the size of the Umbrella and upon finding out stated "*nice...leave it there*";
  - (c) on 7 July 2011 Mr Hughes asked Mr Adoboli whether he wanted to "*rebuild umbrella*", and enquired about its size later on in the same day; and
  - (d) on 2 August 2011 Mr Hughes and Mr Adoboli had a conversation about the latter's trading in which Mr Hughes sought to confirm that the Desk still had funds remaining in the Umbrella.
- 4.11. As well as making enquiries about the size of the Umbrella, by February 2011 Mr Hughes began to make suggestions as to how the Umbrella might be funded. On

21 February 2011, 24 March 2011 and 6 April 2011 he suggested to Mr Adoboli how profits from that day's trading should be divided between the Umbrella and the Desk's reported profit and loss.

- 4.12. Mr Hughes and Mr Adoboli discussed how the Umbrella might be used in chat conversations throughout the Relevant Period. For example:
- (a) on 16 February 2011 and 22 March 2011, Mr Hughes suggested unwinding the Umbrella in order to demonstrate to the Firm how profitable the Desk was and consequently how successful the traders had been;
  - (b) on 14 March 2011, Mr Adoboli indicated that he was considering releasing some Umbrella into the Desk's trading book. Mr Hughes suggested not releasing any funds from the Umbrella as the Desk's trading that day had not been "*that bad*";
  - (c) on 29 March 2011, Mr Hughes suggested the release of some profit held in the Umbrella into the Desk's profit and loss to which Mr Adoboli replied "*understood*";
  - (d) on 14 April 2011, Mr Hughes requested some funds to cover a loss he had suffered in his trading, to which Mr Adoboli responded "*you'll get it*"; and
  - (e) on 22 June 2011, when discussing how the Umbrella should be used with Mr Adoboli, Mr Hughes suggested maintaining the Umbrella as the Desk's "*security*".

Mr Hughes' admissions

- 4.13. Mr Hughes made a number of admissions during his disciplinary hearing with the Firm and in interview with the Authority:
- (a) He believed the Umbrella was a buffer of profit Mr Adoboli had not declared and had kept off the books to offset losses at a later stage.
  - (b) He believed that profit and loss should be accurately reported to enable a firm to properly report its financial results. He knew that the Desk's profit and loss was being misstated because of the Umbrella.
  - (c) Mr Adoboli had told him on a number of occasions the amount of profit which had been set aside in the Umbrella.

- (d) He had discussed with Mr Adoboli how much profit should be diverted to the Umbrella.
- (e) He had asked Mr Adoboli for profits from the Umbrella to cover a loss that he had made.
- (f) He believed that the Umbrella would not have been permitted by the Firm. He believed that if the Firm had found out about the concealment of the Umbrella both he and Mr Adoboli would have lost their jobs.
- (g) He should have reported the existence of the Umbrella to senior management but instead chose not to do so in part because he was complicit in the wrongdoing.
- (h) He did not appeal his dismissal because he believed his failure to report the Umbrella was sufficient grounds for it.

*Factual conclusions*

4.14. On the basis of the facts summarised above, the Authority concludes that during the Relevant Period, Mr Hughes:

- (a) was aware of Mr Adoboli's Umbrella;
- (b) ensured he was regularly appraised of its size;
- (c) became actively involved in decisions as to how it was to be funded and used;
- (d) knew that its use misrepresented the Desk's profit and loss;
- (e) knew that it would not have been permitted by the Firm;
- (f) believed that if the Firm had found out about the Umbrella it would have dismissed him; and
- (g) believed that his failure to report the existence of the Umbrella was dishonest.

**5. FAILINGS**

5.1. The regulatory provisions relevant to this Final Notice are set out in Annex A. The Authority has had regard to the guidance set out in its Handbook and other

relevant regulatory provisions when assessing Mr Hughes' fitness and propriety. One of the Authority's considerations in assessing a person's fitness and propriety is that person's honesty.

#### Dishonesty

- 5.2. During the Relevant Period Mr Hughes occupied a position of responsibility on the Desk. He was the most senior trader on the Desk. In those circumstances he should have acted as a role model to the other traders on the Desk.
- 5.3. On the basis of the facts and matters set out above, the Authority concludes Mr Hughes' conduct in relation to the Umbrella was dishonest. When Mr Hughes became aware of the Umbrella's existence he did not report it to the Firm. Instead, over the course of nine months he became actively involved in how it would be funded and used, and he ensured that he was kept regularly appraised of its size.
- 5.4. Throughout the Relevant Period Mr Hughes was aware that the Desk's profit and loss was being misstated and that this sort of profit smoothing was impermissible. He believed that had the Firm found out about the concealment of profits he would have lost his employment. Despite this he chose not to report the existence of the Umbrella to his superiors.
- 5.5. When the Firm did find out about the Umbrella, Mr Hughes was dismissed for gross misconduct. He admitted that his complicity in the scheme prevented him from reporting the matter to the Firm.
- 5.6. Mr Hughes accepts that his failure to report the Umbrella was wrong and that he was aware at the time that it was wrong. He was aware that his failure to report such conduct by a colleague was a serious infringement of his own responsibilities to the Firm.

#### Mr Hughes' fitness and propriety

- 5.7. Having had regard to:
  - (a) the relevant regulatory provisions set out in Annex A;
  - (b) the facts relevant to Mr Hughes' honesty set out above;
  - (c) the seniority of his role;
  - (d) the period over which the conduct persisted; and
  - (e) his dismissal for gross misconduct;

the Authority considers that Mr Hughes is not a fit and proper person to perform functions in relation to any regulated activity carried on by an authorised or exempt person due to a lack of honesty.

## **6. SANCTION**

- 6.1. One of the Authority's statutory objectives as set out at section 1D of the Act is to protect and enhance the integrity of the UK financial system. The Authority's effective use of its power under section 56 of the Act to prohibit individuals who are not fit and proper from carrying out functions in relation to regulated activities helps the Authority to achieve its statutory objectives.
- 6.2. When an individual such as Mr Hughes, occupies a position of trust and displays a lack of honesty the potential risk to the integrity of the UK's financial system is great. Mr Hughes' failure to inform the Firm of the Umbrella's existence prevented the Firm from identifying Mr Adoboli's unauthorised trading, which ultimately caused losses of \$2.3 billion.
- 6.3. Mr Hughes' conduct is so serious that Mr Hughes should be the subject of a full prohibition order preventing him from performing any regulated activity.

## **7. PROCEDURAL MATTERS**

### **Decision maker**

- 7.1. The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.
- 7.2. This Final Notice is given under, and in accordance with, section 390 of the Act.

### **Publicity**

- 7.3. 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.



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

**Authority contacts**

- 7.5. For more information concerning this matter generally, contact Costas Mavrides (direct line: 020 70663220) of the Enforcement and Financial Crime Division of the Authority.

Matthew Nunan

Financial Conduct Authority, Enforcement and Financial Crime Division

## **ANNEX A**

### **RELEVANT STATUTORY PROVISIONS**

1. The Authority's operational objectives established in section 1D(1) of the Act include protecting and enhancing the integrity of the UK financial system.
2. The Authority has the power, pursuant to section 56 of the Act, to make a prohibition order against an individual prohibiting that individual from performing a specified function, any function falling within a specified description, or any function, if it appears to the Authority that the individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person.

### **RELEVANT HANDBOOK PROVISIONS**

#### **Relevant Rules and Guidance**

3. The section of the Handbook entitled "FIT" sets out the Fit and Proper test for Approved Persons. The purpose of FIT is to outline the main criteria for assessing the fitness and propriety of a candidate for a controlled function. FIT is also relevant in assessing the fitness and propriety of an individual who is not an approved person.
4. FIT 1.3.1G provides 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 (i) honesty, integrity and reputation, (ii) competence and capability, and (iii) their financial soundness.
5. In determining a person's honesty, integrity and reputation, FIT 2.1.1G provides that the Authority will have regard to all relevant matters including but not limited to, those set out in FIT 2.1.3G. FIT 2.1.3G includes whether the person has been dismissed, or asked to resign and resigned, from employment or from a position of trust, fiduciary appointment or similar (FIT 2.1.3G(11)).

### **OTHER RELEVANT REGULATORY PROVISIONS**

#### **Authority's policy for exercising its power to make a prohibition order**

6. The Authority's approach to exercising its powers to make prohibition orders is set out in the Enforcement Guide ("EG").
7. EG 9.1 provides that the Authority's power under section 56 of the Act to prohibit individuals who are not fit and proper from carrying out controlled functions in relation to regulated activities helps the Authority to work towards achieving its operational objectives. The Authority may exercise this power to make a prohibition order where it considers that, to achieve any of those 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.
8. EG 9.4 sets out the general scope of the Authority's powers in respect of prohibition orders, which include the power to make a range of prohibition orders depending on the circumstances of each case and the range of regulated activities to which the individual's lack of fitness and propriety is relevant.

9. EG 9.17 to 9.18 provide guidance on the Authority's exercise of its power to make a prohibition order against an individual who is not an approved person. The Authority will consider the severity of the risk posed by the individual and may prohibit the individual where it considers this is appropriate to achieve one or more of its statutory objectives.
10. When considering whether to exercise its power to make a prohibition order against such an individual, the Authority will consider all the relevant circumstances of the case. These may include, but are not limited to, the factors set out in EG 9.9.
11. EG 9.9 states that, when deciding whether to make a prohibition order against an approved person and/or withdraw his approval, the Authority will consider all the relevant circumstances of the case which may include, but are not limited to, the following factors:
  - a. the relevance and materiality of any matters indicating unfitness (EG 9.9(5));
  - b. the length of time since the occurrence of any matters indicating unfitness (EG 9.9(6));
  - c. the severity of the risk which the individual poses to consumers and to confidence in the financial system (EG 9.9(8)); and
  - d. the previous disciplinary record and general compliance history of the individual including whether the FCA, any previous regulator, designated professional body or other domestic or international regulator has previously imposed a disciplinary sanction on the individual (EG 9.9(9)).