PROHIBITION ORDER – whether Applicant was a fit and proper person - whether Applicant lacked honesty and integrity – no – whether prohibition order should prohibit the Applicant from performing any function (a total prohibition) – no – or whether prohibition order should prohibit the Applicant from performing any management or controlled function (a partial prohibition) – yes – Financial Services and Markets Act 2000 ss 2 and 56; FSA Handbook FIT 2.1

THE FINANCIAL SERVICES AND MARKETS TRIBUNAL

STEPHEN ROBERT ALLEN

Applicant

-and-

THE FINANCIAL SERVICES AUTHORITY

Respondent

Tribunal: DR A N BRICE (CHAIRMAN)
MR RUTHVEN GEMMELL
MR KEITH PALMER

Sitting in London on 28, 29 and 30 September and 1 and 2 October 2009

Roderick Abbott Counsel, instructed by Messrs Segens Solicitors, for the Applicant

Iain Quirk Counsel, instructed by the Financial Services Authority, for the Authority

DECISION

The reference

1. Mr Stephen Robert Allen (Mr Allen) referred to the Tribunal a Decision Notice made by the Financial Services Authority (the Authority) on 16 May 2008. The Decision Notice informed Mr Allen that the Authority had decided to prohibit him from performing any function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm.

2, The Authority gave the Decision Notice because it was of the view that Mr Allen, who was a director of a firm of insurance brokers called Fabien Risk Services Limited (the firm), knew, or was reckless, that between 6 September 2004 and 19 September 2005 the firm had used clients' money improperly and, in permitting that to continue, had acted without honesty and integrity. It followed that he was not a fit and proper person to perform functions in relation to regulated activities carried on by authorised persons.

3. Mr Allen denied that he had known, or had been reckless, that the firm had used clients' money improperly.

The legislation

4 Section 56 of the Financial Services and Markets Act 2000 (the 2000 Act) provides:

> **"(1) Subsection (2) applies if it appears to the Authority that an individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person.**
>
> **(2) The Authority may make an order (a "prohibition order") prohibiting the individual from performing a specified function, any function falling within a specified description, or any function.**
>
> **(3) A prohibition order may relate to:**
> **(a) a specified regulated activity, any regulated activity falling within a specified description or all regulated activities;**
> **(b) authorised persons generally or any person within a specified class of authorised person."**

5. The Authority's Handbook states at FIT 1.3.1 that the Authority will have regard to a number of factors when assessing the fitness and propriety of a person and that the most important considerations will by the person's (1) honesty, integrity and reputation; (2) competence and capability; and (3) financial soundness. It is the first of those considerations which is relevant in this reference.

The issues

6. The Authority argued that, because Mr Allen had not acted with honesty and integrity, he was not a fit and proper person within the meaning of section 56(1) and so should be prohibited from performing any function in relation to any regulated activity carried on by any authorised person. (This was referred to at the hearing as a total prohibition.)

7. Mr Allen accepted that he should have exercised closer scrutiny over the accounting processes of the firm, and to that extent had failed in his duties as a director of the firm, and so should be prohibited from exercising any management or controlled function. (This was referred to at the hearing as a partial prohibition). However, he argued that he had not acted dishonestly, or with a lack of integrity, and therefore a total prohibition would not be appropriate.

8. The Authority accepted that, if Mr Allen had acted with honesty and integrity but had lacked competence and/or capability, then the appropriate order would be a partial, and not a total, prohibition.

9. Thus the issues for determination by the Tribunal were:

(1) whether Mr Allen was a fit and proper person to perform functions in relation to regulated activities and, in particular, whether, between September 2004 and September 2005, he knew, or was reckless, that the firm had used clients' money improperly and, in permitting that to continue, had acted without honesty and integrity; and

(2) whether Mr Allen should be prohibited from performing any function (a total prohibition) or from performing management or controlled functions (a partial prohibition).

The evidence

10. Thirteen bundles of documents were produced. Constant reference was made at the hearing to bundle 1 (the 13 key emails) and to bundle 4 (the witness statements). Very little reference was made to the other bundles.

11. Mr Allen gave oral evidence on his own behalf and oral evidence on behalf of Mr Allen was also given by Mr John Freudenthal who is a chartered accountant who had provided accountancy services to the firm. Witness statements containing evidence on behalf of Mr Allen had been signed by Mr Richard Anthony Bollard and by Mr Roy Langman, who is a director of R. L. Langman Insurance Brokers Limited, Mr Allen's current employer. The Authority indicated that they did not wish to question Mr Bollard or Mr Langman and so their evidence was accepted as unchallenged evidence without the need for their attendance at the hearing.

12 Oral evidence on behalf of the Authority was given by Mr Robert Stephen Kimbell, who is employed by the Authority and who has expertise in the operation of the insurance market and the handling of clients' money. Oral evidence on behalf of the Authority was also given by Mr Michael Seaman who, between July 2002 and July 2005, was employed by the firm. Witness statements containing evidence on behalf of the Authority had been signed by Ms Katherine Braddick and Ms Eleanor Linton both of whom are employed by the Authority. The evidence in these statements was not disputed and Mr Allen indicated that he did not wish to question these witnesses. Accordingly, their evidence was accepted as unchallenged evidence without the need for their attendance at the hearing. Witness statements containing evidence on behalf of the Authority, and signed by Mr Shane Garvey, the chairman and chief executive of the firm, by Mr Lee Goddard, the accounts manager of the firm, and by Ms Annette May Greenhill who, from November 2001 until March 2004 was a director of the firm, were also included in the bundles.

The facts

13. From the evidence before us we find the following facts.

The firm

14. The firm was established in September 2001 as an insurance mediation firm. The business of the firm was to act as insurance brokers introducing clients who required insurance cover to insurers who would provide that cover. An insurance broker's clients are the people who buy the policies; the insurers are not normally the broker's clients. The firm dealt primarily in professional indemnity insurance for solicitors and for other small to medium-sized professional firms.

15. When the firm was established there were three directors, one of whom was Mr Garvey the others being Ms Annette Greenhill and Mr Stuart O'Brien. Mr Freudenthal joined the firm in January 2002 and initially worked full-time. He assisted in setting up the accounts systems for the new firm and also helped with the administration.

16. In 2002 Mr Goddard became employed by the firm in the role of accounts manager. Both the professional and personal relationship between Mr Goddard and Mr Garvey was close. Mr Goddard had been the best man at Mr Garvey's wedding. He had little knowledge of insurance or accounting and had never done an accounts or book-keeping course. Initially Mr Freudenthal assisted with his training.

The firm's internal accounting procedures

17. Insurance brokers receive their income as fees which usually take the form of brokerage commissions. The firm entered into terms of business agreements with insurers under which the firm became entitled to brokerage commission at an agreed percentage in respect of each premium paid by a client of the firm for an insurance policy which was arranged by the firm. The percentages could differ from insurer to insurer. Normally, when the firm arranged a policy, between an insured person on the one hand and an insurer on the other, the insurer would decide the amount of the premium. The insured person would pay the premium to the firm who would then pay it to the insurer after deducting the brokerage commission which was retained by the firm. Sometimes premiums were paid by clients direct to insurers and the insurers then accounted to the firm for the brokerage commissions.

18. Each terms of business agreement also identified the period within which the firm had to account to the insurer for the premium. Thus, for example, the firm could arrange with a client that the client would pay the premium to the firm within thirty days of the risk being accepted by the insurer whereas the terms of business agreement with the insurer could provide that the firm had to pay the premium to the insurer within sixty days of the risk being accepted. Thus the firm would, at any time, be holding money received from clients which was due to be paid later to insurers.

19. The firm's internal procedure was that, when a client wanted insurance cover, the firm prepared a placing slip. When an insurer signed the placing slip a contract of insurance was formed. The member of staff working on the matter would then prepare an internal instruction note to Mr Goddard setting out the name of the client, the name of the insurer and the premium payable by the client. The firm would send a cover note and an invoice to the client showing the amount of premium due and would state that the amount was payable in, say, thirty days. Mr Goddard would also raise an internal debit note. The debit notes were

numbered sequentially and formed part of the firm's internal accounting procedures. If a debit note were prepared correctly then it would state the date on which the insurance policy started, the amount of the premium payable by the client, the date when the premium was payable by the client, and the amount of the premium that could be retained by the firm as brokerage commission.

20. Thus when payment from the client for the premium was received, it should have been possible to identify how much had to be paid to the insurer and how much could be retained by the firm. However, at the time of the preparation of the debit note the part of the premium which could be retained by the firm as brokerage commission might not in fact be known. Also, quite frequently the debit notes did not tie up with the actual transactions because mistakes had been made and in these cases Mr Goddard had to have discussions with the insurers to reconcile the necessary entries. Also, some premiums were received on a block basis from agents and the agent might pay one lump sum which then had to be allocated to individual clients and reconciled. We accept the evidence of Mr Allen that Mr Goddard was rarely up-to-date with the accounting entries and that matters requiring reconciliation and allocation had to wait until Mr Goddard got round to doing them.

The GISC rules

21. On its establishment the firm became a member of the General Insurance Standards Council (GISC). GISC promulgated rules about clients' money. One rule was that clients' money had to be kept in a separate bank account called an IBA (insurance bank account). (Brokers would also have an office bank account which would hold the monies belonging to the firm from which expenses, including salaries, would be paid.) The GISC rules provided that the IBA had to be used for receiving premiums and for paying moneys to insurers.

22. Rule 1.5.5 of the GISC Rules provided that brokerage commissions could not be transferred from the IBA to the office account "before the time in which, in accordance with the accounting policies adopted by the intermediary, the amount may be brought into account as income of the intermediary". In practice this meant that brokerage commissions could be transferred from the IBA to the office account either when the premiums had been received from the clients or when the premiums had been earned but not yet received if the firm's accounts were prepared on that basis. Rule 1.6 provided that the firm had to ensure that the amount in the IBA was greater than the amount due to insurance creditors. Rule 1.7 provided that, if a firm became aware of any deficiency, it had to take steps to restore the required position. The effect of rule 2 was that there should be no overdraft on the IBA bank account.

23. The firm had at least one office bank account (called a general account) and at least two client bank accounts (called the IBA account) one in sterling and one in euros. The office bank account had an overdraft limit of £25,000. The client bank account (the IBA account) was never overdrawn at the bank. We did not see the firm's internal books and records but, from the evidence we did see, we conclude that separate internal books and records were kept for the office account on the one hand and for clients' money on the other.

Mr Allen joins the firm

24 Mr Allen was born in 1963 and commenced work in 1982 as a Lloyds broker. He has worked in that capacity since then and specialises in professional indemnity insurance. Before joining the firm he had not been a company director and had had no training in accounting matters.

25 In or about July 2002 Mr Allen and Mr Seaman joined the firm as employees to work as brokers. (Both Mr Allen and Mr Seaman had worked together at another firm of insurance brokers.) At about the same time Mr O'Brien left the firm following a disagreement with Mr Garvey. During the time which is relevant in this reference (September 2004 to September 2005) the number of employees of the firm, including Mr Garvey, Mr Goddard, Mr Seaman and Mr Allen, was in the region of between eight and eleven. Mr Allen became a director of the firm on 1 October 2002 and that was his first appointment as a company director. The other two directors were then Mr Garvey and Ms Greenhill.

26. On 25 June 2003 abbreviated accounts of the firm for the year ending on 30 September 2002 were audited and signed. The balance sheet showed fixed assets of £52,909 and current assets of cash at the bank and debtors of £744,624 but creditors of £792,332. The authorised share capital was £100,000 of which £10,000 was allotted and fully paid. The profit and loss account recorded a loss of £53,464. Thus the audited accounts for the first year of trading showed that the firm was trading at a loss

The move to Romford

27. Some time in 2003 the firm moved its administrative and accounting functions to Romford and Mr Freudenthal then ceased to work for the firm on a regular basis but occasionally helped out for short periods thereafter. Mr Goddard, Mr Seaman and two other employees were located in Romford. Mr Allen and Mr Garvey with two or three other employees were located in the City of London so that they could have ready access to underwriters and other insurers. Mr Garvey visited the Romford office frequently but Mr Allen very rarely visited the Romford office.

28. When he joined the firm Mr Allen did not deal with financial matters and saw his role as primarily introducing business. He left the day-to-day running of the firm and the finances to Mr Garvey who dealt with Mr Goddard. For example, although he was a signatory for cheques on the bank accounts Mr Allen did not have a password to operate the internet banking facility which was operated by Mr Garvey and Mr Goddard. Mr Goddard sent financial information on a regular basis to Mr Garvey but, before September 2004, Mr Allen was not automatically sent copies of the financial information.

Mr Allen is called the managing director

29. From 23 February 2004 Mr Allen was called the managing director of the firm. However his functions were not defined and his responsibilities did not change. He did not control staff or assume financial responsibilities. Mr Garvey continued to control the financial side of the firm and the running of the firm and Mr Allen worked as an insurance broker and brought in the business and income. Mr Allen was not kept fully informed about the firm's financial position and had to ask Mr Goddard for financial information on more than one occasion.

30. In 2004 a dispute arose between Mr Garvey and Ms Greenhill (who was one of the original directors of the firm). Ms Greenhill left the firm within the context of litigation which cost the firm a significant amount both in lawyers' fees and in staff time which would otherwise have been spent generating business. Mr Allen attributed some of the firm's continuing financial difficulties to this litigation and thought that its end would see an improvement in the firm's finances. As part of the agreement which ended the litigation Ms Greenhill returned her shares to the firm and other senior members of the staff purchased those shares. This gave Mr Allen some comfort as to the firm's financial prospects. At this

time most members of the firm were aware that the firm had cash flow problems as on occasion staff salaries would be paid late.

2004 –The firm applies for authorisation

31. Before 2004 the Authority had started to plan to regulate general insurance business. Draft rules were prepared concerning client assets and client money and, after wide consultation, were finalised in February 2004 with the intention that they would come into force in January 2005. These rules are now found in the Authority's Handbook at CASS (Client Assets). The relevant extracts are set out at paragraphs 43 and 44 of this Decision. The Authority's rules continued to provide for the segregation of clients' monies but also provided that a broker could only transfer brokerage commission from his client bank account to his office bank account after the commission had been received. This was a major change from the GISC rules which, in certain circumstances, allowed commission to be transferred before it was received if it had been earned. After the Authority's rules were published, firms which wished to conduct general insurance business after 14 January 2005 could apply to become authorised by the Authority.

32. Accordingly, in early July 2004 the firm applied to the Authority for authorisation. The form of application was signed by Mr Garvey and Mr Allen who were then the two senior officers of the firm. The form contained a declaration that the signatories would notify the Authority if there was a change to the information given and a declaration that the signatories understood that the firm must ensure that it and its appointed representatives were able to comply, and would comply, with the 2000 Act and the Authority's Handbook from the date of authorisation.

33. On 24 September 2004 abbreviated accounts of the firm for the year ending on 30 September 2003 were audited and signed. The balance sheet showed fixed assets of £52,909 and current assets of cash at the bank and debtors of £1,190,936 but creditors of £1,283,927. There was a loss on the profit and loss account of £108,097. Thus the audited accounts showed that the firm was continuing to trade at a loss. Mr Allen was aware that the firm faced financial difficulties and that there was an overdraft limit on the office bank account. However he did not think that this represented a lack of long-term viability as the business of the firm was expanding.

34 On 4 October 2004 Mr Garvey and Mr Allen signed a guarantee and indemnity in favour of Lloyd's TSB. The amount of the guarantee and indemnity was £55,000 and was in respect of an overdraft facility on the office bank account of £25,000 and a bank loan. The liability of Mr Garvey and Mr Allen under the guarantee and indemnity was joint and several.

35. At some time before December 2004 Mr Martin Webster was appointed as a non-executive director and company secretary of the firm. The directors of the firm were then Mr Garvey, Mr Allen and Mr Webster.

The key emails

36. Between 6 September 2004 and 17 August 2005 Mr Allen received copies of thirteen emails sent by Mr Goddard to Mr Garvey. These emails attached documents containing financial information. The relevance of these emails is that they represented the evidence relied upon by the Authority to prove that Mr Allen knew, or was reckless, that clients'

money was being misused by the firm. They were referred to at the hearing as the key emails and they were sent on:

1. 6 September 2004
2. 15 December 2004
3 28 February 2005
4. 7 March 2005
6. 13 April 2005
7 12 May 2005
8 23 May 2005
9. 3 June 2005
10. 14 July 2005
11. 29 July 2005
12. 3 August 2005
13. 17 August 2005.

37. Each email contained similar financial information. We understand that emails were sent to Mr Goddard on an approximately weekly basis but not all were copied to Mr Allen. The first two emails were received by Mr Allen when the firm was regulated by GISC and before the firm was regulated by the Authority.

The two emails before the firm was authorised

38. The first email (dated 6 September 2004) was sent by Mr Goddard to Mr Garvey with a copy to Mr Allen. The message was:

> "Just to keep you both up to date attached are the necessary spreadsheets and info."

39. The attachments to the first email were (1) a document called "Shane's update"; (2) a document called a list of outstanding payments; (3) a list headed IBA account receipts; and (4) a list headed September's bills. The first attachment was referred to frequently at the hearing and we append the relevant extracts as an Annex to this Decision.

40. The second attachment to the email of 6 September 2004 was called a list of outstanding payments but was in fact a list of outstanding receipts being a list of sums due to the firm from clients. For each entry the list identified the internal debit note number, the amount of premium due and the amount of the brokerage commission due. In respect of five entries (out of a total of about 50) the brokerage commission was shown as £00.00. The third attachment listed 38 payments received by the firm from clients between 2 August 2004 and 6 September 2004 by reference to numbered debit notes but no total was shown. The fourth attachment listed twenty amounts which appeared to be cheques drawn by the firm, and direct debits due by the firm, in July and August 2004. The total of these amounts was shown as £50,506.56. Also shown were amounts for salaries for ten employees, including Mr Allen, Mr Garvey, Mr Goddard and Mr Seaman. The total shown for monthly salaries was £22,964.83.

41. The second email (dated 15 December 2004) was sent by Mr Goddard to Mr Garvey with a copy to Mr Allen. The message stated that, on the outstanding monies list, three amounts due had not been added to the list "though £7,300 had been drawn so far on the NACFB so that will need to be taken off the £20,000 or so brokerage due. This was used to cover business charge cards and the other direct debit ... ." The first attachment to the email showed a negative balance on office account of - £24,903.12 and showed that the total

required to clear cheques sent out, including the overdraft facility, was £54,226.05. The IBA balance was shown as £152,214.39 and the amount "owed to IBA" was shown as £141,965.

January 2005– authorisation by the Authority

42. On 14 January 2005 the firm became authorised by the Authority as an insurance mediation firm with permission to hold clients' money. On the same date Mr Garvey and Mr Allen became approved persons, Mr Garvey was approved to perform the significant influence controlled functions of CF1 (Director); CF3 (Chief Executive) and CF8 (Apportionment and Oversight). Mr Allen was approved to perform the director function (CF 1). In oral evidence Mr Seaman denied that he acted as compliance officer but the documentary evidence indicated that a number of persons regarded Mr Seaman as performing that function and we prefer the documentary evidence which was consistent.

43. On authorisation the GISC rules ceased to apply to the Applicant and the rules promulgated by the Authority applied in their place including the Authority's rules about clients' money. The rules were contained in the Authority's Handbook at CASS. CASS 1 sets out some general principles and CASS 5 contains some provisions which apply to client money and insurance mediation activities. The relevant provisions of CASS 5.4 are:

> **"CASS 5.4 Non-statutory client money trust**
> CASS 5.4.1G (1) CASS 5.4 permits a firm ... to declare a trust on terms which expressly authorise it, in its capacity as trustee, to make advances of credit to the firm's clients. ...
>
> (2) CASS 5.4 does not permit a firm to make advances of credit to itself out of the client money trust. Accordingly, CASS 5.4 does not permit a firm to withdraw commission from the client money trust before it has received the premium from the client in relation to the non-investment insurance contract which generated the commission. "

44. The relevant provisions of CASS 5.5 are:

> **"CASS 5.5.2G** One purpose of CASS 5.5 is to ensure that ... client money is kept separate from the firm's own money. Segregation, in the event of a firm's failure, is important for the effective operation of the trust that is created to protect client money. The aim is to clarify the difference between client money and general creditors' entitlements in the event of the failure of the firm.
>
> **CASS 5.5.3R** A firm must .. hold client money separate from the firm's money.
>
> **CASS 5.5.16R** (1) A firm may draw down commission from the client bank account if:
> (a) it has received the premium from the client ... and
> (b) this is consistent with the firm's terms of business which it maintains with the relevant client and the insurance undertaking to whom the premium will become payable;
> and the firm may draw down commission before payment of the premium to the insurance undertaking provided that the conditions in (a) and (b) are satisfied.
>
> **CASS 5.5.62G**(1) In order that a firm may check that is has sufficient money segregated in its client bank account ... to meet its obligations to clients it is required periodically to calculate the amount which should be segregated (the client money requirement) and to compare this with the amount shown as its client money resource. This calculation is, in the first instance, based on the firm's accounting records and is followed by a reconciliation with its banking records. A firm is required to make a payment into the client bank account if there is a shortfall or to remove any money which is not required to meet the firm's obligations.

CASS 5.5.63R (1) A firm must, as often as is necessary to ensure the accuracy of its records and at least at intervals of not more than 25 business days:

(a) check whether its client money resource ... on the previous business day was at least equal to the client money requirement ... as at the close of business on that day; and

(b) ensure that:

(i) any shortfall is paid into a client bank account by the close of business on the day the calculation is performed ... .

(2) A firm must within ten business days of the calculation in (a) reconcile the balance on each client bank account as recorded by the firm with the balance on that account as set out in the statement ... used by the bank with which that account is held.

CASS 5.5.65R The client money resource, for the purposes of CASS 5.5.65R(1)(a) is

(1) the aggregate of the balances on the firm's client money bank accounts as at the close of business on the previous business day ... .

CASS 5.5.66R A firm's client money (client balance) requirement is the sum of, for all clients, of the individual client balance calculated in accordance with CASS 5.5.67 ...

CASS 5.5.67R The individual client balance for each client must be calculated as follows~;

(1) the amount paid by the client to the firm (to include all premiums); plus

(2) the amount due to the client (to include all claims and premium refunds); plus

(3) the amount of any interest or investment returns due to the client;

(4) less the amount paid to insurance undertakings for the benefit of the client (to include all premiums and commissions due to itself (i.e. commissions which are due but have not yet been removed from the client account);

(5) less the amount paid by the firm to the client (to include all claims and premium refunds);

and where the individual client balance is found by the sum (1) +(2) +(3) – (4) +(5)."

45. Thus the rules make it clear that client money is to be kept separate from the firm's money; that a firm may withdraw commission from a client money bank account only where the premium has been received from the client; that at intervals of not less than 25 days the firm is required to check that the amount of money in its client bank account is equal to all the amounts which must be held there for all clients and, if it is not, ensure that any shortfall is paid into the bank that day; and at the same intervals the firm should reconcile the balance on the client account in the firm's internal records with the balance shown on the bank statement.

46. The firm held client money under a non-statutory trust in accordance with the provisions of CASS 5.4. Mr Allen knew that the client account rules made by the Authority provided that brokerage commission could not be transferred from client account to office account until the premium and the brokerage had been received and paid into the client account (but he also thought that this had been the case under the GISC rules). He also knew about the provisions for periodic client money calculations and bank reconciliations at intervals of not more than 25 days and the obligation to make good any shortfall on the client money account.

The eleven emails after authorisation

47. Mr Allen received no emails from Mr Goddard between 15 December 2004 and 28 February 2005. In February 2005 Mr Allen asked Mr Goddard for a "full copy of all incoming fees and outgoing costs" for February and for the list to be updated and sent to him by the Friday of each following week. Mr Goddard replied on 28 February 2005 (the third email) and sent some attachments which he said were what he sent to Mr Garvey every few days. He added that "Frank's system will do this when the cash allocation has been done but the worry for this is it will tell exactly the current state of the company which will highlight the deficit". ("Frank's system" was a reference to a new computer system which was proposed for the firm.)

48. After he received the third email Mr Allen telephoned Mr Goddard about the reference to the new system showing a deficit and was told that Mr Goddard was merely highlighting the fact that, if he could put all the information into the new system, it could lead to a set of figures which might show a deficit. It appeared to Mr Allen that the reference to a deficit could be a reference to uncollected or unallocated premiums.

49. Three attachments were sent with the email of 28 February 2005, namely (1) a document referred to as Shane's update as at 25 February 2005; (2) a list called outstanding payments which recorded payments due to the firm; and (3) a list of IBA account receipts from 1 October 2004 to 25 February 2005. The first attachment followed a similar format to that used for the first attachment to the email of 6 September 2004 the relevant extracts from which are attached as an Annex to this Decision. The overdraft on general account on 25 February 2005 was - £24,862.53. The actual "IBA balance" was shown as £139,596.53, the amount "owed to IBA" was £140,978.00; and "What IBA balance should be including owed amount" was £280,574.53. The second attachment (the list of outstanding payments) was a list of sums due to the firm from clients. The list identified the premiums, due, and the brokerage commission in respect of each, separately. In respect of between fifty and sixty of these entries the brokerage commission was shown as £00.00. The third attachment (IBA account receipts) recorded a numbered debit note against most, but not all, receipts.

50. After receiving one of the first three emails, most probably after receiving the third email, Mr Allen became concerned that the phrase "owed to IBA" which appeared in the first attachment might mean that clients' money had been misused. Accordingly, he questioned Mr Goddard about the meaning of the phrase and asked if Mr Goddard had taken the money. Mr Allen was told that the phrase referred to items which were still being processed through the accounting system, that is uncollected, unallocated or un-reconciled payments. Mr Allen had no reason to doubt this explanation and trusted what he was told by Mr Goddard. The references in the first attachment to the first three emails of "amount owed to IBA" and "what IBA balance should be" did not appear in any subsequent emails.

The fourth, fifth and sixth emails

51. The fourth email was sent on 7 March 2005 by Mr Goddard to Mr Garvey and Mr Allen. This recorded that the office bank account had an overdraft of - £33,112 and so there was a need to put around £8,200 back into that account (no doubt to maintain the overdraft at just under £25,000). There followed a list of bills due. Under the heading "IBA account" appeared the following ;

> "Currently we have £97,814.51 in the IBA account & £20,762.50 in No. 2 account ... although over the next week we need to pay ... [five payments totalling] £105,710.40. We

have premiums outstanding of around £133,000 and commission to us around £6,300 that I am aware of ... On the euro side outstanding ... commission ... = £5,200."

52. Attached to the fourth email was a list of outstanding payments (being premiums due to be paid to the firm). Almost all the entries showed brokerage commission as £00.00 which explained why the amount of premiums outstanding amounted to almost £133,000 but the amount of brokerage commission due was only "around £6,300".

53. Further emails followed on 13 April 2005 and 12 May 2005. In the message accompanying the email of 12 May 2005 Mr Goddard referred to the "outstanding spreadsheet" (which we take to be a reference to the "list of outstanding payments" which was of course a list of outstanding receipts) and stated that it "shows the premiums and commission owed (if not already drawn) ... I am now in the process of adding the amount owed to the insurers so we know what position the IBA is in."

The seventh to twelfth emails

54. Further emails followed on 17 May 2005 and 23 May 2005. The message with the email of 23 May was:

> "As requested. Please note that the general account was sitting at £30,541.75 as of today so I have drawn £5,600 which will need to be taken from the available monies list where at the moment we have approx £12,165.22 and €5,658.00 available."

55. In the next email which was dated 3 June 2005 the following information appeared:

General account balance	-	41,500.00
IBA Balance		45,305.47
No 2 account		1,500.00
Cheques pending		53,137.73
Actual balance today	-	6,322.26

56. Further emails followed on 14 July 2005, 29 July 2005 and 3 August 2005.

57. Mr Seaman resigned from the firm in July 2005 and there were a number of other staff resignations at about this time.

The events of August 2005

58. Mr Allen was on holiday when the email of 3 August 2005 was sent. Sometime in or about August 2005 Mr Martin Webster, of the firm of Messrs Segens Solicitors, who was then a non-executive director and the company secretary of the firm, was expecting to receive the audited accounts for the year ending on 30 September 2004 but had heard that there could be problems with the finances of the firm. Mr Webster had not received any financial information since a board meeting on 10 December 2004 and he became concerned. On 5 August 2005 he asked Mr Goddard for some specified financial information and requested a board meeting to be held after Mr Allen had returned from his holiday. On 16 August Mr Webster very firmly asked Mr Goddard for further specified financial information. Mr Webster was rightly concerned that the client accounts and other matters should fully comply with the Authority's rules.

59. On 16 August 2005 there was a meeting attended by Mr Garvey, Mr Goddard and Mr Allen. Mr Garvey and Mr Allen instructed Mr Goddard to provide Mr Webster with all the information that he had requested.

60. In reply to Mr Webster's request the thirteenth email (dated 17 August 2005) was sent by Mr Goddard to Mr Webster with copies being sent to Mr Garvey and Mr Allen. The attachments included (1) a draft profit and loss account up to 31 July 2005 which had been prepared by Mr Freudenthal and (2) a document called "a full IBA reconciliation of amounts owed to insurers". The covering message stated: that "the IBA sits at present at £32,185"; that there was currently just over £25,000 fees due to the firm which would be collected the following week; that "the solvency figure is currently being addressed by share purchase"; that the bank overdraft was inside its limit of £25,000; and that the loan had been reduced to £15,500.

61. The first attachment to the email of 17 August 2005 was the draft profit and loss account which was in respect of the period of ten months ending on 31 July 2005. It showed income of £556,095.18 and expenditure of £540,760.00 giving a profit for the period of £15,336.18. The income was mainly derived from brokerage and other commissions and there was also £10,870.18 of interest received (probably from the client money bank account). Expenditure included an amount of £204,327.00 for salaries. The second attachment was headed "Pay insurers" and later "Settle with insurers" and was referred to later as "the IBA reconciliation document". It listed the amounts owed to insurers and gave what appeared to be the names of clients, the names of their insurers, a "date of inception", the debit note reference and the amount of the premium. (No amounts were stated for brokerage commissions). The dates of inception were mainly dates in June and July 2005 and we understand that the date of inception was the date of commencement of cover. The total amount of the premiums listed was £411,167.47.

62. On 19 August 2005 a board management meeting was held attended by Mr Garvey, Mr Allen and Mr Webster. Mr Webster had prepared an agenda in advance of the meeting. Item 2 of the agenda was "Chairman's report of P & L and IBA figures" and item 7 was "FSA compliance and solvency account". After the meeting a minute was prepared by Mr Webster. The minute for item 2 referred to the profit and loss account and the IBA reconciliation document as sent on 17 August 2005 and stated: "Shane Garvey confirmed that both documents were accurate and a true reflection of the current position of the company". The minute went on to state that the auditors were dealing with the audit and they had carried out three weeks' work on the current year's accounts; they had completed the bank reconciliations and needed to complete certain other details. The minute concluded by stating that "Martin Webster made it clear that by his email leading up to the email from Lee Goddard with the figures of 17 August 2005 all he wanted to do was make sure that there were no problems on the figures and it was confirmed by Shane Garvey that there were none." The minute for item 7 recorded that that item had been "dealt with above".

The events of September and October 2005

63. On 19 September 2005 Mr Allen resigned from the firm.

64 On 30 September 2005 the firm ceased to trade.

65. On Saturday 30 September 2005 Mr Allen received a letter dated 27 September 2005 from a firm called Saturn, an underwriting agency. The letter stated that Saturn understood

that there was a serious shortfall in the firm's client account. Saturn also informed the Authority of their concerns on the same day (27 September 2005). When Mr Allen received the letter from Saturn he became concerned and on Monday 2 October 2005 he telephoned the Authority. He attended for a voluntary interview the next day and then or later supplied the Authority with copies of some of the key emails.

66. On 19 October 2005 the firm went into creditors' voluntary liquidation with an estimated deficiency of £701,128 in respect of non-preferential creditors. The sum owed to insurers was £469,741.00 less about £8,500 held in the client money bank account. Thus there was a substantial deficiency on the client money bank account. Mr Allen paid the firm's bank about £34,000 under the guarantee and indemnity that he had signed on 4 October 2004. To do this he had to take out an additional mortgage on his house.

The Authority's investigation

67. Following the liquidation the Authority commenced an investigation. On 19 September 2007 the Authority issued a Final Notice to Mr Garvey. The Final Notice recorded that the investigation had established that Mr Garvey had responsibility for overseeing the firm and its finances but that the directors' and senior managers' functions had not been defined; that Mr Garvey had knowingly authorised the wrongful withdrawal of clients' money from the IBA and the use of that money to keep the firm trading, including the payment of salaries and expenses; that Mr Garvey had knowingly authorised and colluded in the deliberate misrepresentation of the firm's true financial position through the preparation of false and misleading accounting records; and that Mr Garvey had failed to inform the Authority when he knew or ought to have known that the firm was in breach of its financial resources requirements. A total prohibition order was made against him.

68. On the same date (19 September 2007) the Authority issued a Final Notice to Mr Goddard. It was recorded that the investigation had established that Mr Goddard had known since September 2004 that the IBA account had been used to run the firm's business; that from at least December 2004 Mr Goddard had known that there was a deficit in the IBA account of approximately £142,000 and that by May 2005 the firm's financial position had continue to deteriorate; that Mr Goddard had knowingly complied with instructions authorising the wrongful withdrawal of clients' money from the IBA and the use of that money to keep the firm trading; and that Mr Goddard had knowingly colluded and participated in the deliberate concealment and misrepresentation of the firm's true financial position through the preparation of incomplete and therefore misleading accounting records. A partial prohibition order was made against Mr Goddard prohibiting him from performing any controlled function involving the exercise of significant influence over any authorised person in relation to any regulated activity.

69. Mr Garvey and Mr Goddard currently practise as estate agents.

Mr Allen's present employment

70. Mr Allen is now employed by R. L. Langman Insurance Brokers Limited as a specialist professional indemnity broker. He is not an approved person and his employment does not involve any management or controlled functions. His work is supervised by a director and all accounting functions are handled independently by a separate accounting department. In particular, Mr Allen does not handle clients' money. Mr Langman and his fellow directors are aware of the allegations made about Mr Allen and are more than happy

for him to continue to work for their company. Mr Langman has a high regard for Mr Allen's honesty and integrity.

71. On 11 August 2008 Lloyd's TSB, the firm's bank, wrote to Mr Allen confirming that clients' bank accounts had to be kept in credit at all times; that all the firm's client bank accounts had been kept in credit; and that it was not possible for any client bank account to run with any kind of overdraft facility. The letter continued:

> "In view of the continued excess on the main bank account it is purely down to Mr Allen's intervention that the accounts were brought into some kind of order and payments were stopped to avoid going over the agreed overdraft facility. Mr Allen was the only representative [of the firm] to respond to my calls with regard to the accounts activity. Mr Goddard was contacted on a regular basis but had to refer back to Mr Garvey at all times.
>
> Having now worked with Mr Allen for 18 years it is the opinion of Lloyds TSB that he is a trusted individual who has banked personally with us for some twenty years and always maintained an impeccable account. "

The arguments

72. For the Authority Mr Quirk accepted that the burden of proof lay on the Authority to prove that the Applicant was not a fit and proper person and that the standard of proof was the balance of probabilities, bearing in mind that the more serious the allegation the less likely it was that the event occurred and so the more cogent was the evidence required to prove it. He went on to argue that all the evidence pointed to the conclusion that Mr Allen knew, or was reckless, that there was a misuse of clients' money. Mr Allen knew that the financial situation of the firm was dire and he knew or was reckless to the fact that there was a risk that clients' money would be used to fund the business of the firm. Mr Quirk also argued that, after reading the key emails, Mr Allen knew that money was owed to the IBA account; that it had been transferred to office account and used to pay for the firm's office expenses; and that there was insufficient money in the office account to make good the shortfall. He argued that the entries of 00.00 for brokerage commission on the list of outstanding payments meant that brokerage commission had been transferred to the firm's office account before it had been received from the clients. That meant that ultimately there had been insufficient funds in the client account to pay the premiums which were due to insurers.

73. Mr Quirk referred to section 2 of the 2000 Act and relied upon the regulatory objectives of market confidence and the protection of consumers. He referred to the Authority's Handbook at FIT 2.1 which summarised the matters that the Authority would take into account in determining a person's honesty, integrity and reputation. He referred to Chapter 9 of the Authority's Enforcement Guide which set out the Authority's policy relevant to prohibition orders and these included whether a person was fit and proper by reference to his honesty, integrity and reputation. Mr Quirk cited *Hoodless and Blackwell v The Financial Services Authority (*2003) Tribunal Decision No. 007 and *Vukelic v The Financial Services Authority (*2009) Tribunal Decision No. 067 for the principles that knowledge was a different concept from recklessness; that there could be recklessness without knowledge; and that there could be a lack of integrity without dishonesty. He cited *Rayner and Townsend v The Financial Services Authority (*2004) Tribunal Decision No. 009 at paragraphs 101 and 103 for the principle that it was not appropriate to make a partial prohibition order limited to

management and controlled functions in a case where the facts demonstrated a serious lack of integrity.

74. For Mr Allen Mr Abbott argued that the issue before the Tribunal was whether Mr Allen had been complicit in the misuse of client money and that was a matter of fact. Although it had since been established that Mr Garvey and Mr Goddard had misused clients' money held by the firm, Mr Allen's case was that he did not know that that was happening. The Authority relied mainly on the content of the key emails but the context in which they were sent was also relevant and that context included the personalities involved. Further, in considering the emails themselves it was necessary to bear in mind that the question for determination was not what the emails meant but what Mr Allen thought that they meant at the time that he received them. It was also necessary to consider the other evidence before the Tribunal and, in the light of all the evidence, to decide whether Mr Allen was dishonest or lacked integrity. He submitted that the evidence made it clear that Mr Allen was honest and that he was a man of integrity and he referred to the evidence of Mr Langman and the fact that Mr Allen had paid the money owing to the bank which he had guaranteed and had mortgaged his house to do that.

75. As to recklessness Mr Abbott distinguished *R V G* [2004] 1 AC 1034 which related to criminal acts and which did not translate easily into a regulatory context where omissions rather than acts were in issue. Finally, Mr Abbott argued that a partial prohibition was the appropriate sanction. It would recognise that Mr Allen had failed in his duty as a director and would adequately protect market confidence and the interests of consumers as well as permitting Mr Allen to earn his living doing the only work in which he had expertise.

Reasons for decision

76. The first issue for determination in this reference is whether Mr Allen is a fit and proper person to perform functions in relation to regulated activities and, in particular, whether, between September 2004 and September 2005, he knew, or was reckless, that the firm had used clients' money improperly and, in permitting that to continue, had acted without honesty and integrity.

77 In considering this issue we first identify the relevant statutory and regulatory provisions and the authorities cited to us so as to identify the legal principles which we should apply. In the light of those principles we then review the oral and documentary evidence before us, especially the key emails. We then reach our conclusion on the first issue.

The statutory provisions

78. We have set out the provisions of section 56 of the 2000 Act in paragraph 4 of this Decision. That section provides that the Authority may make a prohibition order where it appears that an individual is not a fit and proper person to perform functions in relation to a regulated activity. It follows that our primary task is to decide whether Mr Allen is a fit and proper person to perform functions in relation to regulated activities.

79. The relevant parts of section 2 of the 2000 Act provide:

> **"2(1) In discharging its general functions the Authority must, as far as is reasonably possible, act in a way-**
>
> **(a) which is compatible with the regulatory objectives, and**
>
> **(b) which the Authority considers most appropriate for the purpose of meeting those objectives.**

(2) The regulatory objectives are-

(a) market confidence;

(b) public awareness;

(c) the protection of consumers; and

(d) the reduction of financial crime."

80. Like the Authority we also must act in a way which is compatible with the regulatory objectives and the two objectives which are relevant in this reference are market confidence and the protection of consumers.

The regulatory provisions - FIT

81 The Authority's Handbook at FIT 1.3.1 states that the Authority will have regard to a number of factors when assessing the fitness and propriety of a person and that the most important considerations will by the person's (1) honesty, integrity and reputation; (2) competence and capability; and (3) financial soundness. This reference only concerned the first factor, namely honesty and integrity.

82. FIT 2.1.1 provides that, in determining a person's honesty, integrity and reputation, the Authority will have regard to all relevant matters including those set out in FIT 2.1.3. FIT 2.1.3 sets out thirteen matters to which the Authority will have regard and the following are relevant in this reference:

> "(5) whether the person has contravened any of the requirements and standards of the regulatory system ... ;
>
> (6) whether the person has been the subject of any justified complaint related to regulated activities; ...
>
> (9) whether the person has been a director, partner, or concerned in the management of a business that has gone into insolvency, liquidation or administration while the person has been connected with that organisation or within one year of that connection; ...
>
> (13) whether, in the past, the person has been candid and truthful in all his dealings with any regulatory body and whether the person demonstrates a readiness and willingness to comply with the requirements of the regulatory system and with other legal regulatory and professional requirements and standards."

83. Mr Allen was a director of the firm for three years before it went into liquidation and it went into liquidation very shortly after he ceased to have any connection with it. That therefore is a factor to which regard must be had in determining his honesty and integrity. The application of the other factors in FIT 2.1.1 will depend upon our analysis of the evidence.

The regulatory provisions – the Enforcement Guide

84. Chapter 9 of the Authority's Enforcement Guide relates to prohibition orders and paragraph 9.5 reads:

> "9.5 The scope of a prohibition order will depend on the range of functions which the individual concerned performs in relation to regulated activities, the reasons why he is not fit and proper and the severity of risk which he poses to consumers or the market generally."

85. The relevant parts of paragraph 9.9 of Chapter 9 provide:

> "9.9 When it decides whether to make a prohibition order against an approved person ... the FSA will consider all the relevant circumstances of the case. These may include, but are not limited to those set out below ...
>
> (2) Whether the individual is fit and proper to perform functions in relation to regulated activities. The criteria for assessing the fitness and propriety of approved persons are set out in FIT 2.1 (Honesty, integrity and reputation); FIT 2.2 (Competence and capability) and FIT 2.3 (Financial soundness).
>
> (3) Whether, and to what extent, the approved person has:
> (a) failed to comply with the Statements of Principle issued by the FSA with respect to the conduct of approved persons; or
> (b) been knowingly concerned in a contravention by the relevant firm of a requirement imposed on the firm by or under the Act (including the Principles and other rules) .... .
>
> (7) The particular controlled function the approved person is (or was) performing, the nature and activities of the firm concerned, and the markets in which he operates.
>
> (8) The severity of the risk which the individual poses to consumers and to confidence in the financial system."

86. Paragraph 9.11 indicates that it is not possible to produce a definitive list of matters which might be taken into account when considering whether an individual is a fit and proper person but paragraph 9.12 gives some examples of the types of behaviour which have previously resulted in a decision to issue a prohibition order. These include: providing false or misleading information to the Authority; severe acts of dishonesty e.g which may have resulted in financial crime; serious lack of competence; and serious breaches of the Statements of Principle for approved persons.

The authorities

87. *Hoodless and Blackwell* at paragraph 16 records the principle that, before there can be a finding of dishonesty, it must be established that the defendant's conduct was dishonest by the ordinary standards of reasonable and honest people and that he realised by those standards that his conduct was dishonest. Paragraph 17 records the principle that a person cannot escape a finding of dishonesty because he sets his own low standards and does not regard as dishonest what he knows would offend the normally accepted standards of dishonest conduct. Paragraph 19 states that integrity involves the application of objective ethical standards and connotes moral soundness, rectitude and steady adherence to an ethical code. A person lacks integrity if unable to appreciate the distinction between what is honest or dishonest by ordinary standards.

88. *Vukelic* at paragraph 16 records the principle that the Tribunal is free to make its own determination of whether or not a person is fit and proper taking account of the matters referred to in FIT 2.1.3 and is entitled to reach its own conclusions on grounds not necessarily involving dishonesty. Paragraph 23 states that the Tribunal did not disagree with the statement about integrity which appeared in paragraph 19 of the Decision in *Hoodless and Blackwell* but did not take it as a comprehensive test; integrity was a concept which was elusive to define but readily recognisable by those with special knowledge and/or experience

in a particular market. In paragraph 73 the Tribunal recognised that recklessness was a relevant factor in deciding whether a person is fit and proper and stated:

> "We do not consider that, given the limitations on the quantity and quality of the material available and the way in which justice requires us to approach the question, we can justly reach that conclusion [that the applicant had acted dishonestly]. However we have no doubt that he was reckless."

89. In subsequent paragraphs the Tribunal expressed the view that a lack of experience was a reason to be wary (in that case of substantial business carrying potential regulatory risks) (paragraph 75); that to turn a blind eye to the obvious, and to fail to follow up obviously suspicious signs is a lack of integrity (paragraphs 93 and 119); and that it is reckless knowingly to take an unreasonable risk (paragraph 94).

90. We adopt all those principles.

The oral evidence

91. We found Mr Allen to be an honest and credible witness and accept most of his evidence which was generally consistent. We deal below with his evidence about whether he read the first two pages of the email dated 3 June 2005. In July 2009 Mr Allen commissioned a polygraph report which was annexed to his witness statement; we have not relied upon that report in reaching our Decision. We found Mr Freudenthal to be an honest, straightforward and credible witness and accept his evidence.

92 We found Mr Kimbell to be an honest witness and accept his evidence of fact about the operation of the insurance market and the rules about holding client money. Mr Kimbell also expressed his opinion about the meaning of the key emails. However, the issue we have to decide is not what the emails actually meant but what Mr Allen thought, or should reasonably have thought, they meant at the time he received them. We have decided that question by reference to all the evidence and all the relevant circumstances. The Authority only relied upon the evidence of Mr Seaman to the extent that it was supported by other evidence and we formed the view that that was the best approach to adopt. Neither Mr Garvey nor Mr Goddard gave oral evidence at the hearing. The Authority indicated that they did not rely on the evidence in their witness statements except to the extent that it repeated evidence in other documents before the Tribunal. In deciding what weight to give to this evidence we also bore in mind that Mr Allen did not have the opportunity to question these witnesses at the hearing. Accordingly we decided to give little weight to the evidence in these statements. The Authority accepted that, apart from Mr Seaman, none of their witnesses was with the firm at the relevant time and so they relied primarily on the documentary evidence and on the evidence of Mr Kimbell.

The documentary evidence

93. The main documentary evidence relied upon by the Authority were the thirteen key emails sent by Mr Goddard to Mr Garvey which were copied to Mr Allen. In particular, the Authority relied upon the first attachment to the emails as showing that the running expenses of the firm exceeded the amount available in the office account to meet them and that the firm's expenses had been met by using clients' money, relying on the phrase "owed to IBA". The Authority also relied upon the zero entries for brokerage commissions in the list of outstanding payments which, they said, proved that amounts had been transferred from the

client bank account to the office bank account in respect of commissions where the premiums had not been received.

94. We have considered the contents of the emails in four stages. First, we remind ourselves of context within which we should consider their contents. We then make some general comments on the quality of the financial information presented in the emails. With that background in mind we then consider the two entries specifically relied upon by the Authority, namely, the "owed to IBA" entries and the zero entries for brokerage commission. Finally we consider the other parts of the individual emails which were relied upon by the Authority.

The context of the key emails

95. The question we have to decide is what Mr Allen knew, or ought to have known, *when he received the emails* that is between September 2004 and September 2005. We therefore have to put out of our minds any evidence which emerged after those dates. In particular we must put out of our minds that, in 2007, Mr Garvey and Mr Goddard admitted that they had misused clients' money. Those subsequent admissions cannot be relevant to Mr Allen's state of mind at an earlier date.

96. The context within which the emails were sent was that they were primarily sent by Mr Goddard to Mr Garvey. Mr Goddard was the accounts manager. Mr Garvey was the chairman and chief executive of the firm. There was a close relationship between Mr Garvey and Mr Goddard. Mr Goddard worked in Romford, where the firm's back office functions took place and no doubt where the firm's financial records were kept. Mr Goddard had no accounting qualifications nor was he a trained book-keeper. Mr Garvey visited Romford. Mr Allen worked as a broker in the City of London and virtually never visited Romford. His main concern was generating business and income. He had no accounting experience and had not previously been a company director. He was not concerned with the accounting processes of the firm. His request in February 2005 for a full copy of all incoming fees and outgoing costs indicated that he was primarily concerned with the profitability of the firm rather than with the details of the accounts. Although after February 2004 Mr Allen was called the managing director of the firm, from the evidence before us we conclude that this title was used to give him added status when representing the firm. In reality, in such a small firm, and with Mr Garvey acting as chairman and chief executive, Mr Allen's role was that of a director particularly concerned with the broking side of the firm's business and not the role one would expect of a true managing director. It is really as a director that he should be judged.

97. It is also relevant that the emails we saw were part of a series sent by Mr Goddard to Mr Garvey which series had commenced before September 2004. After 6 September 2004 some emails were sent to Mr Allen but not all were. The emails were primarily addressed to Mr Garvey who may well have been familiar with their presentation and meaning. The first attachment (of which a copy is attached as an annex to this Decision) was informally called "Shane's update" and so was primarily prepared for Mr Garvey who no doubt understood the relevance of all the entries. We are in the same position as Mr Allen as the only emails we saw were those copied to Mr Allen. When we read them initially, without any explanation as to what they meant, we found them puzzling.

98. Another factor which we bear in mind is that Mr Goddard was rarely up-to-date with the processing of the firm's internal accounting procedures. Also the internal debit notes did

not always tie up with the actual transactions so that they had to be reconciled and, pending reconciliation, the accounting information would not be complete. In the words of Mr Allen "matters requiring reconciliation and allocation had to wait until Mr Goddard got round to doing them".

99. Finally we bear in mind that Mr Garvey later admitted to the Authority that he had knowingly authorised and colluded in the deliberate misrepresentation of the firm's true financial position through the preparation of false and misleading accounting records and that Mr Goddard admitted to the Authority that he had knowingly colluded and participated in the deliberate concealment and misrepresentation of the firm's true financial position through the preparation of incomplete and therefore misleading accounting records. If the firm's accounting records were deliberately false, misleading and incomplete that is part of the context within which the information in the emails has to be considered.

The quality of the financial information in the key emails

100. In considering the quality of the financial information presented in the key emails we begin by examining the first document attached to the first email dated 6 September 2004 which is attached as an Annex to this Decision. We find it hard to categorise this document. Mr Kimbell thought that it was clearly not a client money calculation (and we agree). We call it a statement.

101. This statement has some defects. First, in listing the amounts due from the firm, the three amounts due to the Inland Revenue of £4,000, to Hual UK of £6,914.09, and to Capital Growth of £2,666.66 appear twice and were counted twice in the total of sums due. That puts into question the validity of the other calculations. Secondly, after summarising the amounts due to be paid by the firm there are references to brokerage commissions to be collected followed by three amounts described by reference to the Inland Revenue giving the impression that the Inland Revenue were to pay these amounts to the firm. Mr Kimbell at first read the statement in that way and so did we. However, we were informed at the hearing that those three amounts were in fact owed by the firm to the Inland Revenue and not by the Inland Revenue to the firm. Mr Allen realised that these amounts were owed to the Inland Revenue but this lack of clarity reflects on the quality of the information generally. Mr Kimbell candidly admitted that, at a first reading, he had misinterpreted some of the figures in the statement and so did we.

102. The Authority argued that the fact that the statement attached to each email recorded the balance of the office account as being very near the overdraft limit of - £25,000, together with the other information in each email, indicated that the expenses of the firm exceeded its income. That in turn suggested that the debit balance on office account was only maintained at just under the overdraft limit by means of a topping-up from the client account. However, we agree with Mr Kimbell that the statement by itself does not prove that the firm was in financial difficulties because reference was only made to one "general account balance" which was in overdraft but there was no reference to any other assets. To reach a balanced view it would be necessary to know further financial information including what other assets were available to the firm and that information was not provided in the emails.

103. Mr Allen pointed out that the statement listed all sums due in September but only the amount in the bank account as at 6 September. After 6 September and before the end of the month when all the bills had to be paid further sums would be received. The firm had an annual turnover in the region of £648,000 per annum or £54,000 per month but that

information did not appear from the emails. Mr Allen also knew that the firm received interest on the monies held in the IBA account and that was not shown in the emails either.

104. It is relevant that the emails do not attach copies or extracts from the bank statements relating to the firm's office bank account or client money bank account nor do the emails purport to be summaries of the firm's internal books and records. Mr Allen was able to examine the bank statements on the rare occasions that he visited Romford but on the evidence before us we are unable to find that he saw the firm's internal books and records. We were provided with a bundle containing copies of the firm's bank statements but that bundle was not referred to at the hearing. We did not see the firm's internal books and records.

105. The second attachment to the emails was headed as a list of outstanding payments whereas in fact it was a list of outstanding receipts. That demonstrates a lack of clarity in the presentation of the information. We accept the evidence of Mr Allen that spreadsheets prepared by Mr Seaman for himself and Mr Allen contained more brokerage commission due than that recorded by Mr Goddard on the list of outstanding payments and he knew that the list of outstanding payments was not accurate.

106. In summary, we agree with the evidence of Mr Freudenthal that the financial information contained in the emails and their attachments was at best incomplete and at worst hopelessly confused and could not be relied upon to provide accurate information of the firm's financial position at any one time. The information was a snapshot of some selected figures on particular days. In particular, we are also unable to agree that Mr Allen knew, or should have known, after reading the emails that the debit balance on office account was only maintained at just under the overdraft limit by means of a topping-up from the client account as there could have been other explanations.

107. With those general comments in mind we turn to consider the two specific matters contained in the key emails which were relied upon by the Authority, namely the "owed to IBA" entries and the zero entries for brokerage commission on the list of outstanding payments.

"Owed to IBA"

108. The Authority argued that the phrase "owed to IBA", which appeared in the first attachment to the first three emails, must have conveyed the meaning to Mr Allen that clients' money had been misused. (A copy of the first attachment to the first email is annexed to this Decision). When we originally read the emails that is what we thought also.

109. However, we accept the evidence of Mr Allen which was that initially he thought that the phrase meant unpaid premiums. We have also found as a fact that after receiving one of the first three emails, most probably after receiving the third email, Mr Allen became concerned that the phrase "owed to IBA" might mean that clients' money had been misused. Accordingly, he questioned Mr Goddard about the meaning of the phrase and asked if Mr Goddard he had taken the money. Mr Allen was told that the phrase referred to items which were still being processed through the accounting system, that is uncollected, unallocated or un-reconciled payments. Mr Allen had no reason to doubt this explanation and trusted what he was told by Mr Goddard. In view of the fact that Mr Goddard was never up-to-date with his accounting entries we do not consider that it was unreasonable for Mr Allen to take this view at the time.

110. It is perhaps significant that the references in the attachments to the first three emails of "amount owed to IBA" and "what IBA balance should be" did not appear in any subsequent emails. We do not know why as we did not receive oral evidence from Mr Goddard. (One possibility might be that Mr Goddard did not wish Mr Allen to make any further enquiries and, if that were the case, it would point towards the conclusion that Mr Allen did not know what was going on. However, as this is only speculation we do not rely upon it.)

111. We have also been assisted by the evidence of Mr Freudenthal (which we accept). Mr Freudenthal gave evidence that it could not be assumed that the entries of "owed to IBA" and "what the IBA balance should be" indicated that those amounts had been taken from the client bank account as they could have represented outstanding premiums owing to the firm the amounts for which, when they were paid to the firm, would be paid into the IBA account. He was of the view that all the attachments when read together did not point to the conclusion that the firm had extracted sums from the IBA account for use in its business.

112. We also bear in mind that, at the dates of the first two emails, the relevant rules were the GISC rules and not the rules of the Authority. Accordingly it was permissible at that time for the firm to transfer brokerage commission from client account to office account before it was received if it had been earned.

113. Bearing in mind the context within which the emails were sent, the quality of the financial information they contained, and the other evidence before us we conclude that the phrase "owed to IBA", which appeared in the first attachment to the first three emails, did not constitute cogent evidence that Mr Allen knew or should have known, at the time he received the emails, that clients' money had been misused. (Mr Allen now accepts, with hindsight, that that the phrase "owed to IBA" which appeared in the statement attached to the first three emails meant that money was owed to the client account.)

The zero entries for brokerage commission

114. The Authority argued that the zero entries for brokerage commission, which appeared on the outstanding payments list, must have conveyed the meaning to Mr Allen that clients' money had been misused. (The outstanding payments list was in fact a list of sums due by clients which had not been received by the firm and should perhaps have been called an outstanding receipts list.)

115. However, we accept the evidence of Mr Allen that he did not interpret the zero entries as representing brokerage commissions taken before the premiums had been received. Rather he understood that the entries represented figures in respect of unallocated or un-reconciled items which had not yet been processed through the accounts system either because Mr Goddard did not know how much the amount of the brokerage commission would be or because he was not up to date with his record keeping.

116. Mr Freudenthal also thought that that was a possible interpretation of the zero entries. His evidence was that originally problems had been created by a failure by Mr Goddard to enter client cases onto the firm's accounting system in a timely manner. That meant that invoices, cover notes and statements were issued to clients in an overdue or incorrect fashion which could result in late payment. To correct these problems Mr Goddard was instructed to enter all cases into the system even if they were still being processed. So the zero entries

might mean that the commission had not become due. Also, if the firm had entered into terms of business with an insurer then the amount of commission would probably be known but if there were no terms of business with that insurer the amount might not be known.

117. Mr Kimbell thought, when he first read the emails, that the zeros could have represented commission taken before the premiums had been received but, as he had not analysed the books and records of the firm, he could not be sure. We note that Mr Allen did not see the books and records of the firm either and it is relevant that Mr Allen worked in the City of London whereas the books and records were kept in Romford. We did not see the firm's books and records either.

118 Bearing in mind the confusing state of the financial information contained in the emails we are unable to find that the zero entries for brokerage commission constituted cogent evidence that Mr Allen knew or should have known that money was being extracted from the client money bank account in respect of commissions before the money had been received.

119. Having considered the "owed to IBA" entries and the zero entries for brokerage commission we finally turn to consider the other parts of the individual emails which were relied upon by the Authority.

15 December 2004

120. The message in the second email, dated 15 December 2004, stated that, on the outstanding monies list, three amounts due had not been added to the list "though £7,300 had been drawn so far on the NACFB so that will need to be taken off the £20,000 or so brokerage due. This was used to cover business charge cards and the other direct debit ... ." The Authority argued that these words conveyed the meaning that brokerage commission of £7,300 had been transferred from client account to office account before the premiums had been received.

121. Mr Allen told us that NACFB was the National Association of Commercial Finance Brokers and that was the only client of the firm who paid adjustable premiums. Between two and three hundred finance brokers were insured under a block policy for which a minimum premium was paid at the start. As new members joined the Association during the year additional premiums would be charged. At the time of the second email about £7,300 additional premium was due which Mr Goddard had drawn. Also, the whole policy was due for renewal which meant that a further premium of £20,000 was also due.

122. In considering this email we note that, at its date, the relevant rules which applied were the GISC rules which permitted the transfer of commission which had been earned but not received. If the email did convey the meaning that £7,300 had been transferred from client account to office account in respect of brokerage commission which had been earned but before the premium had been received then that was not then a breach of the rules.

28 February 2005

123. The Authority argued that the reference in the covering email of 28 February 2005 to the fact that the new computer system would "highlight the deficit" pointed to the conclusion that Mr Allen was aware that the client money account was in deficit.

124. We have already found as a fact that, after he received the third email, Mr Allen telephoned Mr Goddard about the reference to the new system showing a deficit and was told that Mr Goddard was merely highlighting the fact that if he could put all the information into the new system it could lead to a set of figures which might show a deficit. It appeared to Mr Allen that the reference to a deficit could be a reference to uncollected or unallocated premiums. Other possibilities mentioned at the hearing were that the reference was to a deficit on office account or to the fact that premiums were owing which had not been collected or to the fact that Mr Goddard had not processed all the relevant entries.

125. In view of the letter dated 11 August 2008 from Lloyds TSB, confirming that clients' bank accounts had to be kept in credit at all times; that all the firm's client bank accounts had been kept in credit; and that it was not possible for any client bank account to run with any kind of overdraft facility; we conclude that any deficits mentioned by Mr Goddard in his emails as deficits on client account were deficits in the firm's books and records and not overdrafts on the client bank account (the IBA). We also conclude that the deficiencies in clients' money later recognised by Mr Garvey and Mr Goddard were effected by transfers out of the client money bank account (the IBA account) to the office bank account while leaving the client money bank account in credit at all times (although with a balance which was lower than it should have been). However, this information is not clear from a bare reading of the emails and, in our view, would not have been obvious to Mr Allen when he received them.

7 March 2005

126. The Authority relied upon the email of 7 March 2005 as showing that the firm had to make payments during the month of approximately £82,000 and could only expect to receive income of about £10,500. In the light of what we have said about the quality of the financial information presented with the emails we accept the evidence of Mr Allen that the figures in the email for income did not include the full picture. Further, the fact that there might have been difficulties in balancing the office account does not automatically lead to the conclusion that there were difficulties with the client account.

12 May 2005

127. The Authority relied upon the email message of 12 May 2005 and the reference to "premiums and commission owed if not already drawn" as indicating clearly that commissions were being drawn by the firm before premiums were received. We accept the evidence of Mr Allen that he did not read the phrase in that way and the words "already drawn" could refer to brokerage commission which had been received and paid into the IBA bank account and then properly transferred to the office account. We also accept the evidence of Mr Freudenthal that, as Mr Goddard was not a qualified accountant and as his terminology was not exact, he would not have drawn any conclusions but would have asked Mr Goddard for an explanation of the phrase used.

23 May 2005

128. The Authority argued that the message to this email made it clear that the overdraft on the office bank account had been exceeded by about £5,600 and we agree. However, Mr Quirk went on to argue that the £5,600 which had been drawn down must have come improperly from the IBA account because, if the other sums mentioned in the email were legitimately due, they would all have been already transferred. We do not consider that that inference can fairly be made.

3 June 2005

129 There was an issue of credibility about this email. Mr Allen initially stated that he had not received the first and second page of the email and its attachments. However, we find that he did receive them because he asked questions about them three days later. We regard this inconsistency as an understandable lapse of memory when recalling events which occurred four years ago and not as undermining the overall credibility of Mr Allen's evidence.

130. The Authority relied upon the entry in the email of 3 June 2005 which showed a negative IBA balance of -£6,332.26 as conveying the meaning to Mr Allen that the IBA account was in deficit. We have already found that the IBA bank account was never overdrawn and we do not read the figures mentioned as necessarily meaning that the client account in the firm's books of account was in deficit. No explanation was given for the meaning of the entry for "cheques pending". If these were cheques which had been signed on behalf of the firm but not sent then the intention might have been for them to be sent when further sums had been received. We agree that if the amounts in "cheques pending" were owed to insurers then the money ought to have been in the IBA account unless the amounts were due to the insurers before they were received from the clients but we had no evidence about that. Once again we remark that the statement was just a snap shot of the position on one day and did not clearly convey the meaning that the there was insufficient monies in the client bank account.

17 August 2005

131. The Authority also relied upon the email of 17 August 2005 and its attachments. We first note that on the face of the draft profit and loss account (which was prepared by Mr Freudenthal) the firm appears to be trading at a profit after the payment of salaries, albeit a small profit. The Authority argued that the second attachment made it clear that there was a shortfall in the client bank account of £411,000 owed to insurers, In the second attachment, of the amounts owed to insurers, it is not clear to us on the face of the document that the amounts mentioned had been received by the firm. The dates of inception (which were the dates of the commencement of cover) were all in July and August 2005 and it was not clear that the premiums had been received. It seems to us that this document could have been taken to be another in the series of "lists of outstanding payments" which were in fact lists of outstanding receipts (and its appearance was similar to those lists). Mr Kimbell appeared to think that this was the case. If the document were read in that way then it would not cause any alarm and there was nothing on the face of the documents to indicate that the amount in the client bank account was insufficient to account to insurers for all the premiums which had in fact been received by the firm.

132. It is also relevant that the email of 17 August 2005 and its attachments were considered at the board management meeting of 19 August 2005 and the minutes of that meeting indicate that Mr Webster's concerns about the financial position of the firm had been allayed.

Conclusion

133. The question we have to determine is whether Mr Allen is a fit and proper person to perform functions in relation to regulated activities and, in particular, whether, between September 2004 and September 2005, he knew, or was reckless, that the firm had used clients' money improperly and, in permitting that to continue, had acted without honesty and integrity. The burden of proof lies on the Authority to prove that Mr Allen is not a fit and proper person and that the standard of proof is the balance of probabilities, bearing in mind that the more serious the allegation the less likely it was that the event occurred and so the

more cogent was the evidence required to prove it. The Authority allege that Mr Allen was dishonest and that is a very serious allegation.

134. We do not consider that the documentary evidence of the emails provides the requisite cogent proof that Mr Allen knew, or should have known, when he read them that the firm had used clients' money improperly. Given the severe limitations on the quality of the financial information presented by the emails we cannot reach the conclusion that he was dishonest. On the evidence before us, neither do we consider that he knowingly took an unreasonable risk and so we conclude that he was not reckless. We have considered separately whether Mr Allen, while not being reckless in September 2004, was reckless to ignore the cumulative warning signs which were present by July 2005. However, by that time Mr Webster had become involved and preparations were being made for the meeting on 19 August when matters were to be discussed. We now know (although there is no evidence that Mr Allen knew at the time) that Mr Garvey and Mr Goddard colluded in the deliberate misrepresentation of the firm's true financial position through the preparation of false and misleading accounting records and that may explain the outcome of the meeting on 19 August. Bearing in mind the minute of that meeting it looks as if the records misled Mr Webster and could have misled Mr Allen. On the evidence before us, therefore, we are unable to conclude that Mr Allen became reckless from about July 2005. And we do not consider that Mr Allen turned a blind eye to the obvious or failed to follow up suspicious signs. The information conveyed by the emails was not obvious although it can now be understood with hindsight. Mr Allen did follow up suspicious signs by enquiring about the references to "the deficit", to the phrase "owed to IBA", and to the zero entries for brokerage commission. Accordingly we conclude that he did not act without integrity.

135. Mr Allen candidly admitted that, with hindsight, he should have considered the emails more carefully. He accepted that his lack of knowledge of the firm's bank accounts was a neglect of his duties and that he had failed in his duty as a director of the firm. The Authority accepted that, if Mr Allen had acted with honesty and integrity but had lacked competence and/or capability, then the appropriate order would be a partial, and not a total, prohibition. We agree and are of the view that the appropriate order is a partial prohibition.

136 We therefore determine the issues in the reference as:

(1) that between September 2004 and September 2005 Mr Allen did not know, nor was he reckless, that the firm had used clients' money improperly and that he did not act without honesty and integrity; and

(2) that because Mr Allen failed in his duties as a director of the firm he should be prohibited from performing any management or controlled functions.

Direction

137. Section 133(4) of the 2000 **Act** provides that, on a reference, the Tribunal must determine what, if any, is the appropriate action for the Authority to take in relation to the matter referred to it. Section 133(5) provides that, on determining a reference, the Tribunal must remit the matter to the Authority with such directions (if any) as the Tribunal considers appropriate for giving effect to its determination.

138 We determine that the appropriate action for the Authority to take in relation to this matter is to make a partial prohibition order. We therefore remit this matter to the Authority

and direct that the Authority should only make a prohibition order prohibiting Mr Allen from performing any management or controlled function.

139. This is a unanimous decision.

DR A N BRICE

CHAIRMAN

RELEASE DATE:

Stephen Robert Allen
FIN/2008/0010
25.11.09

Annex

Relevant parts of a document referred to as "Shane's update" being the first attachment to the email of 6 September 2004

Fabien Risk Services Limited

General Account balance 6th September			**- 24,014.64**
...			
Money transferred from IBA /Euro today to be added			**1,666.06**
when taking into account £25000 overdraft		**c**redit avail	**2,651.42**
Cheques/transfers Outstanding			
Cheques that will hit this week		chq no	
	nacfb dinner	940	188.00
	viking direct	928	712.36
	beaufort	910	4,313.42
cheques to be sent today			
19th May tax month 1 2004	**Inland Revenue**		**4,000.00**
very urgent letter threatening action	**Hual UK**		**6,914.09**
	Capital Growth		**2,666.66**
Direct debits due in September	**BT**	**5th**	**345.00**
	Freedom	**6th**	**22.50**
	Foot Ellis	**14th**	**700.00**
	Premium	**19th**	**5,058.33**
	Pitney	**19th**	**31.67**
	Orange	**26th**	**600.00**
19th May tax month 1 2004	**Inland Revenue**		**4,000.00**
Now	**Hual UK**		**6,914.09**
	Capital Growth		**2,666.66**
	Total		**39,132.78**
Total required to clear all of above			**36,481.36**
Fabien Brokerage to be collected (see outstanding list) ...			**17,181.45**
inland revenue 19th June tax month 2 2004			**14.128.93**
inland revenue 19th July tax month 3 2004			**14.545,15**
inland revenue 19th August tax month 4 2004			**14.542.67**
Bond Pearce claims admin			**2,937.00**
			46,153.75
IBA Balance 6/9/04			**137,797.88**
cheques pending			24,936.66
Owed to IBA ()			**144,298.00**
What IBA balance should be			**257,159.23**
Saturn owed (ITEC)			**5934.64**