

Regulatory Breach



ST. PAULS CHAMBERS

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Pop goes the Weasel and other Credit Crunch tales.

In this ‘credit crunch’ edition, we look at the new approach of the SFO following the appointment of Richard Alderman as Director in April 2008. Although politicians and the media seem to be clamouring for action against rogue institutions and bankers, the new dawn that has been alluded to seems to involve civil recovery rather than prosecution for dishonesty. Time will tell whether or not this approach proves to be effective as a deterrent against fraudulent conduct.

We look at an interesting development in litigation to unwind these schemes, which results in those who have achieved payouts from the schemes prior to collapse having to return those monies to the liquidator, quite a frightening consequence for those who have gone on to spend their return thinking that the company had been trading honestly.

‘Pop goes the weasel’, the old children’s nursery rhyme has its origins in pawnbroking. This is one area of the market which is undergoing substantial growth during the recession, we look at regulation of credit businesses under the Consumer Credit Act 1974.

We also welcome the introduction of the Carbon Ready newsletter and website which can be found at www.carbonready.co.uk. The latest edition deals with the Climate Change Act 2008, Obama’s commitment to lower US car emissions, and a fall in carbon pricing due to our old friend the credit crunch!

Jeremy Barnett

Stop Press!!

We are delighted to announce the arrival of Simon Myerson QC who joins the Regulatory Group in chambers TODAY.

Simon has experience in Health and Safety and a range of Professional Disciplinary Jurisdictions including Public Inquiries and hearings before the Solicitors Disciplinary Tribunal.

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“new, faster approach to tackling fraud”



Jeremy Summers

Partner, Business & Regulatory Investigations, Russell Jones & Walker

Almost as soon as 2009 had started, the Serious Fraud Office announced it was to investigate potential UK criminality arising from the Madoff scandal. Richard Alderman hailed the investigation as an example of the SFO's “new, faster approach to tackling fraud”.

Since being appointed as the SFO's Director in April 2008, Mr Alderman has made it clear that he favours a more American approach to prosecutions and seeks to lead his organisation into a new, and pro-active, style of combating fraud.

The clearest example yet of that approach has been the ground breaking settlement with Balfour Beatty using Civil Recovery powers that only became part of the SFO's toolbox in 2008. This involved an investigation that started in 2005 and related to the construction of the internationally acclaimed Bibliotheca Alexandria. It was settled in October 2008 with a monetary payment and the SFO accepting that, in all the circumstances, no prosecution of any individual or entity was merited.

In many ways this settlement was analogous to the Deferred Prosecution Agreements now regularly deployed by the US Department of Justice and Securities and Exchange Commission (SEC). Significantly, the facts that Balfour Beatty itself reported its concerns and was willing to allow external monitoring of its ongoing compliance systems were persuasive factors in the SFO's decision.

Mr Alderman has since indicated this is likely to be the template for future enforcement action in suitable cases, whilst also pointing to the fact that the SFO will be devoting significant additional resources to fighting fraud and corruption. The clear message is that companies which fail to demonstrate a new level of corporate responsibility are likely to find themselves in a very uncomfortable position.

The FSA has similarly indicated its intention to use its criminal enforcement powers with more regularity and a number of insider dealing prosecutions are pending. It too would like a more American style toolbox and, in particular, the ability to offer plea bargaining and immunity.

Ironically, as the SFO and FSA seek to embrace the “American model”, the SEC, one of the bastions of that model, has seemingly been caught asleep at the wheel with Madoff. The UK may therefore be about to embrace a system that the US now realises needs urgent repair. 2009 may well be an interesting year.

Jeremy Summers is a partner in the Business and Regulatory Investigation department at Russell Jones & Walker and together with Rod Fletcher represented Balfour Beatty throughout the Bibliotheca investigation.

Penny pinching lands driver in court

A driver is over £7,000 out of pocket after being successfully prosecuted for failing to declare dangerous goods at Dover.

The case relates to an incident on 27th December 2007 at the Port of Dover when a Toyota motor vehicle was “stop checked” by Port of Dover Police in the freight section of the outbound embarkation lane for the Norfolk Line Ferry. The Police Officers discovered that the vehicle was carrying two drums of Cosmocil S Propylene Glycol Dispersant. This product is Class 9 Hazardous Goods. The driver of the vehicle, Stephen Deane, was in possession of the relevant documentation including IMO Dangerous Goods Declaration Transport Documents.

The Police detained Deane and interviewed him under caution for not declaring to Norfolk Line that he was carrying these goods. When interviewed Deane fully admitted withholding the information from Norfolk Line both when purchasing his ticket on line and at the check in booth. His motive was to purchase a ‘tourist ticket’ because it was cheaper. Deane admitted in court that he had bought a tourist ticket for £70 a freight ticket would have cost £170.

Stephen Deane, aged 49 from Glasgow, was fined £2,000 and ordered to pay costs of £5545.28 by Folkestone Magistrates.

Mr. Chris Boreham, Surveyor-in-Charge at Dover Marine Office said:

“The regulations covering dangerous goods on ships exist for the safety of passengers and crew. It is essential that the Master and crew of ferries are aware of what Dangerous Goods their vessel is carrying so that the correct action is taken in the event of an emergency. I would like to thank Port of Dover Police for their assistance in this matter.”

Note

The exporter was a chemical company based in West Yorkshire. However the goods passed to Stephen Deane to transport via three other sub contractors. The method of invoicing each sub-contractor means that each party simply quotes an ‘all in’ price which means that transport ticket costs are hidden within, so no one can readily identify where cheaper tickets were purchased. This matter arose as a result of the self employed driver Deane trying to save or make money

Investors who got out early could still be targets

Jeremy Barnett
St Pauls Chambers

The Madoff Scandal is spawning an array of law suits in the USA and the UK. Suits have been filed by the SEC, investor groups and those against other entities such as feeder funds who introduced their own clients to Madoff, often without notice being given.

Investors who had the good fortune to liquidate their holdings in Bernard Madoff's funds are not necessarily in the clear. If Mr Madoff's investment advisory business turns out to have been, in his own words, a "Ponzi scheme", the people who withdrew funds early could find themselves targeted by a court-appointed trustee.

Another case that appears similar to Mr Madoff's, albeit on a smaller scale, involved Dana Giacchetto, who pleaded guilty in 2000 to defrauding some of his celebrity investors in his Cassandra Group.

The trustee, Robert Geltzer, sued film stars Cameron Diaz, Tobey Maguire, Ben Stiller and Tim Roth, on behalf of investors, to recover funds already paid out to them. Mr Geltzer also sued Michael Ovitz and Ms Diaz's manager, Rick Yorn.

Another attorney, Sidney Liebesman, says if the allegations against Mr Madoff are true, wronged investors could take action against third-party asset managers who recommended putting money into Mr Madoff's funds.

The Securities Industry Protection Corporation (SIPC) could be a source of recovery. SIPC guarantees are limited to \$500,000 per account and legal action against SIPC is often necessary to recover claims. However, SIPC has limited reserves and would not be able to cover billions in losses without a government infusion.

Investors may be vulnerable if they have withdrawn money within the past six years -- the statute of limitations in New York state, where Madoff's company is headquartered, said Susman Godfrey partner Harry Susman. "It's a common thing to happen in a Ponzi scheme when it collapses," Susman said. "If there's any evidence that they knew something was foul when they withdrew the money they would have to give it back in principal as well." But even investors who are forced to disgorge money may get some of it back when the bankruptcy trustee distributes all the collected funds.

EU leaders claims of 'historic agreement on low-carbon future'

Jeremy Barnett
St Pauls Chambers

On December 12, European leaders announced that they were leading the world towards a low-carbon future after sealing an ambitious climate change pact by making generous concessions to the big polluters in European heavy industry. Critics however question the strength of the commitment, saying it is too little, too late.

A two-day summit of 27 government leaders in Brussels ended a two-year effort to agree mandatory reductions in greenhouse gas emissions in Europe and came as a triumph for President Nicolas Sarkozy of France in the closing days of his six-month presidency of the EU who declared: "This council will go down in the history of Europe."

The climate accord orders Europe to cut greenhouse gas emissions by 20% by 2020 compared with 1990 levels. This is to be achieved through national reduction targets which vary among the 27 countries and through a Europe-wide carbon trading scheme in which industries and power plants buy permits to pollute from 2013.

Following German pressure, the rules for the emissions trading scheme (ETS), however, were relaxed to exempt most companies in the processing industries, such as steel and cement, from paying for the permits and power stations in central Europe, mostly coal-fired, were awarded large discounts on the price of carbon.

The decisions also cut CO2 emissions from cars by 19% by 2015, set binding national targets for renewable energy to total 20% of the European energy mix by 2020, encourage the use of "sustainable" biofuels, and order 20% greater energy efficiency by 2020.

Robin Webster, climate campaigner for Friends of the Earth, said: "This could have been one of Europe's finest moments. But huge loopholes allow big energy-users to carry on polluting."

At the United Nations Climate Change Conference, COP 14 at Poznan, all parties agreed that a new framework would be finalised at Copenhagen at the end of 2009. The first draft of will be available at Bonn in June 2009. Important agreements were reached on issues that affect developing countries, including adaption [coping technologies], finance, technology, deforestation and disaster management.

At a side event in Poznan, Lord Stern confirmed that there does seem to be a consensus amongst policies to deal with climate change. He indicated that Obama and Ed Milliband seemed convinced of the case and was confident that substantial progress would be made. Milliband has announced a package which includes provision for 12 pilot projects on carbon capture and storage.

The projects are to be funded from the proceeds of the carbon trading which is supposed to generate tens of billions in revenue by 2020. Under pressure from the British, the summit agreed to double the funding available for these projects.

“Pop goes the weasel”

Fiona Barnett
Walker Morris

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The reluctance of mainstream banks to lend in the credit crunch has created a positive knock-on effect for those involved in the ancient business of pawnbroking. Albemarle and Bond, the UK's biggest pawnbroker which bought rival Herbert Brown in July 2007, reported a gain of 43% in annual revenues, and lifted adjusted profits for the year to 30th June to £10.3 million.

Pawnbroking is a well established form of money lending. There is plenty of evidence to support its existence throughout history. Some sources say it started in 1462, when Franciscan monks established “Banks of Pity” to enable poor people to obtain small collateralized loans. References to pawnbroking however, can even be found in the Bible,

“...no man shall take the nether or the upper millstone to pledge, for he taketh a man's life to pledge”.

...and also in nursery rhymes. Many parents of this generation will be unaware that “Pop goes the weasel,” describes the pawning of a coat to pay for everyday items. To “pop” is the cockney verb, to pawn, and the “weasel” is the “weasel and stoat”, cockney rhyming slang for a coat. Traditionally, items of clothing such as coats were commonly placed on deposit in exchange for cash.

But what has become of the old-fashioned pawnbroking industry, and how is it regulated?

Pawnbroking is essentially a means of obtaining money on credit. The Pawnor (customer) will take an item to “pawn”. The Pawnee (pawnbroker) will assess its value, retain it as security, and lend cash of similar value to the customer. The money must be paid back with interest during or at the end of the agreed term in order to redeem the goods, failing which the pawnbroker can sell or “realise” them to recoup the value of the loan.

Pawnbroking activity is governed by the Consumer Credit Act 1974 (CCA), and regulated by the Office of Fair Trading. The provisions of the CCA which are specific to pawnbroking largely mirror principles set down in the Pawnbrokers Act 1872.

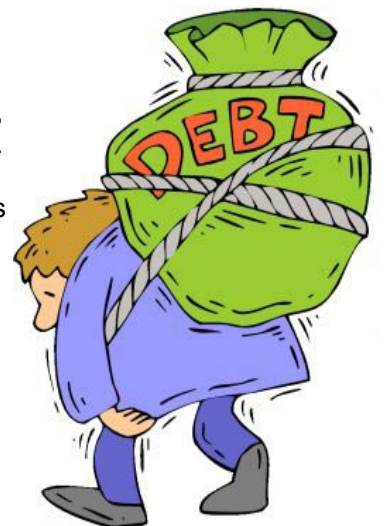
The pawnbroker must give the customer a receipt when he takes an item “in pawn”, and commits an offence if he does not do so. In practice, the pawn receipt and the loan agreement are often one and the same. It is also an offence to take an article in pawn from a minor.

Loan agreements must be for a minimum of six months, during which the customer can redeem his goods at any time and the pawnbroker is not at liberty to sell them. Many pawnbrokers opt for slightly longer agreements; this is because if an agreement is only for 6 months, and the value of the loan is less than £75, the pawnbroker will become the legal owner of the goods if they are not redeemed at the end of the 6 month period. This can have VAT consequences for the pawnbroker if/when he then sells the goods. In all other cases, the pawnbroker can “realise” or sell the goods, but as he does not legally own them, he has no VAT liability on sale.

At the end of the loan period, the customer can redeem his goods at any time until they are sold by the pawnbroker. The pawnbroker commits an offence under the CCA if he refuses “without reasonable cause” to let the customer have his goods back.

If the customer does not redeem the goods, he must (unless specified otherwise) be given notice by the pawnbroker of his intention to sell them with details of the asking price. He (the pawnbroker) must then provide written details of any sale, and following payment of the debt from the proceeds of sale, account for any surplus funds to the customer. If there is a shortfall, the amount of that shortfall becomes the debt from the date of the sale.

Whilst pawnbroking is now fully regulated, it appears that the principles have changed very little throughout history. Current economic trends have however given rise to changes in the type of items pawned. The head of the National Pawnbrokers Association, Des Milligan, reported that one person had recently pawned his Aston Martin for £30,000. On the whole, transactions remain relatively low in value, with jewellery used most commonly as security and approximately 85% of goods being redeemed. The industry seems to have shed its negative image. Customers appreciate that pawnbroking can avoid a spiralling cycle of debt, and enable them to obtain cash quickly, albeit to pay the school fees, keep the bailiffs away, or just to fund a good night out.



New Toy Directive adopted by European Parliament

Jeremy Barnett
St Pauls Chambers

The European Parliament has now adopted the new Toy Safety Directive following months of consultation and revision. It gives consumers assurance that toys sold in the EU fulfil the highest safety requirements world-wide, especially those relating to the use of chemical substances.

Vice-President Günter Verheugen, responsible for enterprise and industrial policy, said: "Children's health and safety is precious and demands the highest possible protection. I am very pleased that the EU has been able to agree within record time on these robust and far reaching rules for safe toys. The new rules incorporate the newest health and safety standards. What legislators can do for children to be safe when playing with toys has been done."

The new legal framework addresses a wide range of issues to ensure that toys do not present any health hazards or risk of injury. It improves the existing rules for the marketing of toys that are produced in and imported into the EU with a view to reducing toy related accidents and achieving long-term health benefits.

New chemical requirements

Chemicals that are susceptible to provoke cancer, change genetic information or harm reproduction, so-called CMR (Carcinogenic, Mutagenic or toxic for Reproduction) substances are no longer allowed in accessible parts of toys. For certain substances like nickel the tolerable limit values have been reduced and those heavy metals which are particularly toxic, like lead or mercury, may no longer be intentionally used in toys. Allergenic fragrances are either completely forbidden, if they have a strong allergenic potential, or have to be labelled on the toy if they are potentially allergenic for some consumers.

Enhanced safety requirements to prevent choking risks

Rules to prevent children from choking or suffocating on parts of toys, especially small parts, are strengthened, *inter alia* to deal with the new risk of toys such as those with suction cups. Toys in or co-mingled with food always need to be in a separate packaging. Toys which are firmly attached to a food product at the moment of consumption (e.g. so called "party lollypops") and which require the food to be consumed before getting access to the toy are prohibited.

Warnings on toys

In order to prevent accidents, warnings need to be marked on toys in a clearly visible, easily legible manner in a language easily understood by consumers. Warnings that contradict the intended use of the toy are not allowed, in particular the warning "not suitable for children under 36 months" on toys clearly intended for this age group. Toys contained in food or co-mingled with food shall bear the warning: "Toy inside; Adult supervision recommended".

Obligations for toy manufacturers and importers

The obligations for toy manufacturers and importers are considerably strengthened. Before a manufacturer tests whether his toy respects the safety requirements of the Directive, he has to carry out a safety assessment of the toy, and establish more comprehensive technical information for all his products, including information on chemicals used, to allow traceability by the market surveillance authorities. Importers must check whether producers have carried out conformity assessment of toys correctly and if necessary must carry out random tests themselves. If toy manufacturers/importers do not produce toys in line with the safety requirements of the Directive, Member States can impose penalties. Toy distributors obligations are also strengthened.

Strong national market surveillance systems

Member States will have to ensure that market surveillance authorities perform adequate checks at the EU external borders and within the EU including visits to premises of all economic operators to ensure that dangerous toys are immediately prohibited or withdrawn. Market surveillance authorities can also destroy toys presenting a serious risk. Thanks to the reinforcement of the market surveillance provisions also the CE marking has been strengthened. It is now required that the CE marking must always be affixed on the packaging if the marking on the toy is not visible from outside the packaging in order.

The New Directive differs from the existing Directive in a number of important ways including;

- Mandatory content of technical files – including a list of components and materials used in the manufacture of toys
- Mandatory sample testing
- Batch, serial or model numbering
- A mandatory EC-Declaration document is defined
- All toys will have to be formally assessed for hazards and risks and the assessment retained in technical files
- New rules for notified laboratories
- New enforcement powers for surveillance authorities
- New chemical requirements for toys including new limits for existing toxic metals and new requirements for other toxic metals – it is estimated that the cost of testing toys will at least quadruple as a result of these new rules
- New chemical requirements with respect to CMR substances, fragrances and toys containing cosmetics.

EU Member States will have 2 years to implement the new directive