

## Beaufort Securities – a gathering storm

by Peter Parry

*The liquidation of Beaufort Securities on the FCA's instruction is targeting the ring-fenced property of thousands of UK private investors, many of whom are now facing losses of up to 40% of the value of their holdings. The liquidator's proposals bring into question the whole system of regulatory and legal protection of investors in the UK. In particular, they suggest that investors' assets which are held in a nominee account are not actually ring-fenced as is widely believed.*

The Financial Conduct Authority (FCA) declared Beaufort Securities Limited (BSL) and sister company Beaufort Asset Clearing Services Limited (BACSL) insolvent on the 2nd March 2018 and PwC were appointed as administrators of BSL and special administrators of BACSL.

On 15th March, PwC confirmed that the ring-fenced property of the Group's clients was held appropriately in accordance with FCA requirements, being approximately £50 million in segregated client money accounts and around £850 million in client-owned securities. On 12th April, PwC noted that client money and client assets were, as at the date of administration, substantially complete save for a very small number of isolated deficiencies. However, the initial estimate of £850 million client assets was reduced to £500m as a result of illiquid / nil value positions. The special administrator stated that the majority of client asset returns will commence September 2018 at the earliest and that around 700 clients with assets valued over £150,000 may experience a loss up to a maximum of 40% on their ring-fenced assets!

PwC is proposing to charge an incredible £100 million for the wind-down over a period of four years. They have provided no justification of either the amount or timeframe for the simple task of transferring an electronic registry of client assets/money to one or more replacement brokers.

Over 14,000 clients invested through Beaufort Securities, an FCA regulated entity, on the assurance that their assets were firewalled per FCA rules precisely to protect them in the event of the broker's insolvency. The suggestion that PwC as Special Administrator can seize client property and treat the owners as creditors of the failed entity makes a mockery of regulatory protections for investors in the UK.

The FCA seems to have allowed Beaufort Securities to continue trading while the FBI carried out an undercover investigation, apparently putting the interests of the FBI ahead of those of UK investors. This calls into serious doubt the FCA's priorities and the regulator's role in protecting domestic savers.

ShareSoc and UKSA are determined to defend the interest of Beaufort clients, and the interests of UK shareholders in general, whose shares are held in nominee accounts and are therefore similarly exposed to the insolvency of their brokers.

ShareSoc has launched a campaign which UKSA is fully supporting with the primary purpose of mounting a legal challenge to the current administration proposals, specifically:

- Refuting the Special Administrator's right to seize ring-fenced client property
- Ensuring proper separation of the liabilities of BSL from those of BACSL
- Questioning the Special Administrator's cost and time estimates in relation to the wind-down of BACSL
- Seeking a transfer of the business of BACSL to an alternative custodian
- Reviewing the actions and motivations of the FCA in this matter
- Lobbying for legislative change to ensure that assets in custody are properly protected

Renowned FT writer and private investor John Lee says: *"I am very happy to endorse the thrust of ShareSoc's campaign. We were all shocked to discover the seeming vulnerability of clients' funds when we thought that they were ring-fenced and protected. This loophole surely has to be closed."*

Details of the campaign can be found here: <https://www.sharesoc.org/campaigns/beaufort-client-campaign/>.

UKSA and ShareSoc have campaigned for many years for legislative change that would result in shares being directly registered in the names of their beneficial owners, rather than via brokers' nominee accounts. Such a system would have prevented the current attack on the private property of the Beaufort group's clients.

## Incentives versus regulation – which would you back?

*by Martin White*

*Regulation isn't what really drives behaviour. Yes sure, it creates work, for the regulators themselves, for those whose job is to follow the regulations, and also for those whose job is to get round the regulations. And then we have the lawyers. What really drives behaviour is incentives. And understanding – or perhaps more appropriately misunderstanding. We need massive reform in both of these. To improve outcomes, it has to be the sort of reform that the corporate establishment will resist strongly.*

In these pages, you will be used to reading about a series of shocking stories. Carillion and Persimmon have been egregious enough and recent enough for Parliament to take an interest. There is a perceived failure in stewardship and reporting on stewardship – and for this boards and the accounting profession are in the frame. However, read the Parliamentary report on Carillion, and look at the recommendations. Guess what – the prescription is the usual one, more regulation, and tougher regulation.

I just don't think there is enough deep thinking within policymaking circles. To fix a problem, you have first to understand it. It's not that people naturally behave badly; it's that the "system" tends to push them towards bad behaviour. What do I mean by this? To me the "system" includes, and is defined by, lots of things including what gets praise (promotion and/or pay and/or keeping the job), and what gets punished (loss of job, bonus disappointment).

Most really bad behaviour seems to have as its immediate cause a mix of greed and fear, driven by what gets the "well done". And as an intelligent owner, it's difficult to see how these incentives are really in the long-term interest of the company. But isn't that exactly what the board should be there to implement? A decently run company will focus not primarily on profit today, and not on the share price, but on things that will enhance the company's future competitive strength, its long-term survival and its long-term ability to generate distributable profits. Identifying companies that think like this is my focus when looking at smaller companies. I like them to care about the business and the team, not just about making money.

I realise I'm no more than touching on the subject here. One of the things that characterises some smaller companies is a strong element of management control. Without this, fear of takeover can lead to an excessive focus on the share price. But there will be an excessive focus on the share price when there is any form of pay that is dependent on share price. I'm coming to the conclusion that we should go back to salaries, with virtually no "performance-dependent" pay. This, of course, would close the door to all those headline-catching pay outcomes – hence the strong resistance I expect from the corporate establishment to any such suggestions.