

Financial Services and Markets

Record FSA Fine for ex-CEO's fraud

On 31 January 2012, the UK Financial Services Authority published findings of fraud and the imposition of a fine of £2,867,000 against Ravi Shankar Sinha, the former chief executive officer of JC Flowers' FSA-regulated European private equity business ("JCF").

Mr Sinha had taken out substantial personal loans to fund co-investments. When the value of those investments fell during the financial crisis, he struggled to make repayments. He funded these repayments by entering into fraudulent schemes, first obtaining a personal loan from one of the fund's portfolio companies, then charging advisory fees to the same portfolio company (paid into his personal bank account), in each case without the knowledge or approval of JCF. In total, Mr Sinha dishonestly obtained €1.548 million in payments from the portfolio company over 8 months.

Mr Sinha has been banned from working in the UK regulated sector in any capacity. It is reported that no criminal prosecution will be brought.

The FSA has made no criticism of JCF. Mr Sinha's conduct was in deliberate breach of the terms of his employment and the firm's policies and procedures. His fraud was identified and brought to the FSA's attention by JCF. JCF has reimbursed the portfolio company for its losses, meaning that there is no loss to the company or fund investors.

Key points

- This appears to have been a straightforward case of fraud by abuse of position. It is notable because of the prominent position that Mr Sinha held at JCF – he was a Managing Director of the firm globally and the most senior executive in Europe.
- This is a record fine imposed on an individual in a non-market abuse case.
- The fine of £2,867,000 comprises disgorgement of the financial benefit of Mr Sinha's misconduct, and a penalty of £1.5m. The FSA imposed the penalty even though it accepted that it would probably result in serious financial hardship. In doing so it states that it took into account:
 - Mr Sinha's level of seniority and the leading position of JCF in the financial services industry;
 - that the misconduct was very serious - concluding that it should not reduce the punitive element notwithstanding that it would probably have the result of making him bankrupt for a second time (his first bankruptcy was discharged in August 2011);
 - that his misconduct resulted in financial detriment to others;
 - that he co-operated with the FSA.

Whilst this case involved fraud, firms and individuals should note that the FSA change in fining policy is resulting in significant fines, including for non-fraudulent conduct.

- This is the second case in a week where the fine takes into account the standing and visibility of the employer in the market (see [Agnew](#)).

- Mr Sinha's representations with a view to reducing the level of the financial penalty included:
 - a suggestion that JCF would have approved the loan and fee arrangements had he sought authorisation (a contention which JCF disputed);
 - an argument that, since he had forfeited the prospect of a substantial carried interest distribution, he had obtained no net benefit from his misconduct; and
 - an objection that, since JCF is suing him, a requirement to disgorge the benefit of his conduct could result in him paying twice.

Key messages

- The FSA clearly states that it makes no criticism of JCF's systems and controls. All regulated firms are required to operate systems and controls to mitigate the risk of internal fraud. Such systems generally include background checks on prospective new hires, rigorous financial control and, in some cases, internal as well as external audit. The case recognises that no system can eliminate fraud risk, but all firms should review their own internal fraud risk assessments regularly to ensure that their anti-fraud arrangements are defensible in the event that they do suffer from an internal fraud.
- In their anti-fraud, conflicts and general risk assessments, private equity and venture capital firms should consider (where relevant) if any personal financial commitments placed on executives by some types of co-investment arrangement could give rise to increased fraud risk. If so, firms need to consider how they monitor and mitigate any such risks.
- Private equity and venture capital firms should also be alive to the risks of fraud involving portfolio companies, particularly if portfolio company financial monitoring is the responsibility of those executives who are themselves in a position to influence the portfolio company.

The Final Notice against Mr Sinha is [here](#).

We regularly advise financial services firms, including private equity houses, on cases of employee misconduct and in relation to anti-financial crime controls. Please follow these links for further information about our [Financial Services and Markets team](#) and [Regulatory Investigations team](#).

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