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## Fears that CHC may not be the only bad apple

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Wealth managers fear failure to see what was going on may mean there are other cases, writes Jon Ihle

The failure of regulators and auditors to spot the systematic and deliberate misuse of client funds at Custom House Capital has raised the question of whether such issues could be more widespread among Irish investment managers.

Figures in the asset management industry are concerned that Custom House might not be the only wealth management firm violating rules on the segregation of client accounts and are worried about the impact of the revelations on the sector.

“The Custom House Capital scandal has the potential to further damage the confidence of the Irish public in financial intermediaries and it’s important that it’s addressed,” said Mark O’Byrne, executive director of Goldcore, a gold brokerage and wealth manager.

One senior figure in the industry, who asked not to be identified, said he believed standards among asset managers were low and that regulation was still too weak to safeguard a sector that has control over billions in savings.

More than €56million of client money at Custom House was misappropriated from cash and equity funds and put into property investments without client knowledge, the High Court-appointed inspectors found.

According to a senior official in the Central Bank, a large number of employees in the company knew exactly what they were doing when they carried out instructions by Custom House directors to raid client funds to prop up other investments. But with one exception in 2009, none blew the whistle. This is borne out by transcripts in the inspectors’ report, in which junior staff said they were intimidated by Custom House chief executive Harry Cassidy who “ruled with an iron fist”.

“Guys in the industry knew something was up at Custom House,” said Kevin O’Doherty, director of regulatory consultancy Compliance Ireland. “Surely if the Central Bank had shut them down earlier, the problem wouldn’t have been as big.”

In the wake of the Custom House revelations, the Central Bank has stepped up its scrutiny of how asset managers handle customer accounts. Proper segregation of client accounts has been a major theme of Central Bank director of enforcement Peter Oakes in the last year, and the regulator has doled out several administrative sanctions for violations.

However, officials acknowledged that it was nearly impossible to prevent abuses completely.

By the Central Bank’s own admission, the worst of Custom House’s violations were not discovered until Appian Asset Management tried to acquire the firm last summer. Even though Central Bank officials and KPMG accountants had been investigating irregularities in one of the firm’s bond funds since early 2009, they missed that tens of millions had been drawn from client accounts without permission and ploughed into international property deals.

In fact, the Central Bank was comfortable enough with Custom House that it granted Appian

takeover approval. Within ten days of taking ownership of Custom House, Appian had uncovered the mess which led to the appointment of inspectors.

The Central Bank is in the middle of a review of how its regulators gather and handle client asset returns, which theoretically should have uncovered the misdeeds at Custom House. A report on the matter is due in January.

Financial Regulator Matthew Elderfield has concentrated Central Bank resources on institutions that either pose a systemic risk or engage in risky activity. In short, the system is designed to guard against another Anglo Irish Bank or Quinn Insurance nightmare. Custom House, as an apparently garden variety asset manager, did not fall into either category.

Goldcore's O'Byrne said the regulator should now bar pension trustees from also offering investment advice, to avoid conflicts of interest. Asset managers should also have to hold client funds with an independent custodian, he said.

Compliance Ireland's O'Doherty said there were "very few" firms with the kind of attitudes that appear to have prevailed at Custom House and that most regulatory breaches were of technical or complex rules. He also said the regulator had a "huge armoury" to deal with violations - it was just a question of using them effectively.

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