CRAZY WORLD

An investigation of the rise and fall of Worldspreads sheds light on the bizarre dealings of the Dublin-based company, writes *Gavin Daly*

August 1, 2007, was an auspicious day for Niall O'Kelly. Worldspreads, the Dublin spread betting group where he was chief financial officer, floated on AIM, the junior market in London, raising £5.77m (€6.7m) to fund expansion.

The company enjoyed a good run as a plc. Its share price more than doubled within a year and Worldspreads had 15,000 clients by 2011.

Then it all fell apart. On March 18, 2012, citing "financial irregularities", the UK's Financial Services Authority (FSA) appointed administrators from KPMG to Worldspreads. They found a £15.5m hole in the client funds held by the firm.

On April 7, more than five years on from the collapse, O'Kelly, 47, was fined £11,900 by the FSA's successor, the Financial Conduct Authority (FCA), and barred from any job in a regulated company. The authority wanted to impose a fine of £468,756 but accepted O'Kelly faced "serious financial hardship".

Lukhvir Thind, a former financial controller at Worldspreads, was fined £105,000 and also barred from regulated companies. The FCA's rulings offer the first comprehensive view into the deception at Worldspreads, described within the company as the "Blackhole".

Founded in Dublin in 2003, Worldspreads offered customers the chance to bet on share prices, sports events, even election outcomes. Its early investors included the former footballer Kevin Moran and the golfer Paul McGinley.

What an outside observer could not know was that some Worldspreads directors and staff had a strategy from the start of taking opposite positions to certain client bets. If a client bet that a share price would rise, for example, the Worldspreads insiders bet that it would fall, or vice versa.

The system, dubbed internal hedging, was fatally flawed. If client bets were unsuccessful, the Worldspreads insider bet would come good; but if the client was right, the insider bet would lose and the participants would have to pay up. "It was a risky and highly unorthodox strategy," said the FCA.

The Worldspreads participants clearly knew the approach was unusual. Instead of using accounts in their own names, they used fictitious client trading accounts and even real client accounts without the clients' knowledge, so the practice was hidden from auditors.

If their bets lost, the money owed was presented as an asset on the Worldspreads balance sheet. But the insiders "did not generally settle losses", the FCA found, so the accounts were misleading.

By the end of March 2006, before the flotation, there was a deficit of almost €518,500 on the internal hedge accounts. From the autumn of that year, Worldspreads was also hiding an internal loan arrangement, where some directors secretly provided personal loans to shore up financial difficulties.

In total, they lent €1.625m to a Worldspreads subsidiary, including €100,000 from O'Kelly. The majority of the money was held in Worldspreads bank accounts but not accounted for as loans or related-party transactions.

In fact, the company's AIM admission document stated there were "no outstanding loans" from any director to any part of the group. If the loans had been disclosed, investors would have had an indication Worldspreads "was not generating enough cash and/or that banks were unwilling to lend" to the group.

The failure to disclose the internal hedging and the directors' loans meant the Worldspreads accounts were "substantially incorrect" and its IPO admission document was "materially misleading", said the FCA. If the document had been accurate, the flotation "might have been delayed or cancelled, or investors might not have purchased shares at all".

Instead, the company was valued at nearly £20m in the IPO. Just 15 days after the float, one of the insider participants described the hedging practice in an internal email as "contrary to all trading standards and ethics for a trading desk".

He added: "I guarantee you there is [not] a single trading desk in the world where traders take part of the book themselves without shareholder approval and proper procedure."

In an email to O'Kelly and others on January 11, 2008, another participant wrote: "Lets not fool ourselves … there will never be any money coming in from [the internal hedging] losses (at least until there is an exit)."

The company motored on regardless, reporting operating profits of £2.9m for the financial year to the end of March 2008. Yet Worldspreads was actually in "severe financial difficulties" and struggling to cover costs.

From January 2008, O'Kelly and Thind were "improperly and secretly" misapplying client money. The FCA said O'Kelly admitted that, by March 2009, the Worldspreads accounts were "misstated, with respect to profit, by €5m".

In internal communications, the gap between the reported finances and the reality, "was referred to as the Blackhole or the You Know What". In 2009, the company got a chance to restructure its finances when it sold off its Irish business, which was renamed Marketspreads, and a small sports unit called Sports Spread (see panel).

O'Kelly is being allowed to pay his fine in instalments because of his straitened finances

While O'Kelly told others at the company that the black hole had reduced to €1.5m, it was soon growing again. From December 2009 onwards, the company did not have enough money to cover the funds it purportedly held for clients.

The financial position became "especially acute" between 2010 and 2011, the FCA found. On February 14, 2011, for example, Thind processed seven payments of £200,000 each from a client account to a company account to meet margin calls on internal bets.

Despite that, the 2010 and 2011 accounts published by Worldspreads "showed strong revenue growth and a cash-rich balance sheet", and analysts published positive research. The FCA found O'Kelly and Thind kept up the illusion by creating fictitious entries, labelled Seg Ireland in the daily client money reconciliation statements.

By March 31, 2011, the client money requirement was nearly £23.6m but Worldspreads had just over £8m. A Seg Ireland figure of £15.5m was inserted to balance the books but there was no Seg Ireland account and no extra cash. It was "entirely fictitious", found the FCA.

For the annual Worldspreads audit, O'Kelly and Thind, who did not personally benefit from the transactions, simply deleted the Seg Ireland entries and reduced the figure for the client money requirement to match the funds that were available.

To back up the false figures, Thind, under O'Kelly's instructions, "amended and deleted individual client cash balances" in the company's trading system reports. The FCA said it had confirmed that O'Kelly and Thind sent the company auditor EY "trading system reports in which individual client cash balances had been materially falsified".

As a result, "all of the public statements that Worldspreads made about its cash position in 2010 and 2011 were false and misleading". The charade ended on March 16, 2012, when Thind went to the Worldspreads board and raised concerns. Shortly afterwards, O'Kelly confirmed Thind's information.

After the FSA was informed, the company's shares were suspended from AIM and it was put into administration on March 18, 2012. In interviews with the FCA, O'Kelly "made full admissions of wrongdoing" and gave a chronology of the abuse from before the IPO to the company's collapse. Thind "provided a prompt and detailed account" of the issues, according to the FCA.

£17.9m

The amount paid in compensation to Worldspreads clients by January 2017

In 2015, EY paid a £2m settlement to the Worldspreads administrators without any admission of liability. By January this year, £17.9m was paid out by the Financial Services Compensation Scheme, an investor compensation fund in the UK, to cover the losses of 3,833 former Worldspreads clients.

The KPMG administrators filed their final progress report on Worldspreads last month and have been discharged from their duties. They have said they will not pursue legal actions against parties connected to Worldspreads, including its former directors and their professional advisers.

Because of his straitened finances, O'Kelly is paying his FCA fine in quarterly instalments of €1,141. His final payment is due in April 2020.

HOW TWO MEN'S BIG BET ENDED UP IN THE BANKRUPTCY COURTS

Worldspreads Ireland was sold to two senior executives, Brian O'Neill and Fergus Rice, in December 2009. The duo, with backing from a number of private investors, agreed to pay €9.2m for the business.

Soon after, the new investors commissioned EY, the company auditor, to conduct a retrospective audit of the 2009 accounts. It found profits at the company , since renamed Marketspreads, had been overstated by €2.5m.

A series of court cases would later hear how O'Neill and Rice diverted more than €1.4m out of Marketspreads Ireland to Sports Spread Betting (Ireland), a company controlled by Rice. According to bank accounts statements, it was alleged that €750,000 was then paid from Sports Spread Betting to Rice and O'Neill's personal accounts.

The executives resigned in June 2011. In April 2012, after the Central Bank of Ireland suspended Marketspreads' trading licence for a period of three weeks, the company raised cash from shareholders, and bought out O'Neill and Rice's 40% shareholding for €400,000. This sum was set against the Sports Spread Betting debt. O'Neill and Rice claimed this was a full and final settlement. The company pursued the men for the outstanding balance, and succeeded in bankrupting the two directors.

Sports Spread continues to trade as sportsspread.com. In 2016, Simon Morehen, a UK customer, sued the company for the return of £15,000 from his account. O'Neill, described in court as a betting consultant to sportsspread.com, said he advised the company that gambling debts and gambling monies were not recoverable under the Gaming and Lotteries Act. Yet the company agreed to return money to Morehen.

Sportsspread.com does not accept bets from customers domiciled in Ireland, according to its website.

Sports Spread Betting (Ireland) is currently listed for strike-off.