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Financial Ombudsman Service

essential reading for financial firms and consumer advisers

in this issue

about this issue

In past issues of *ombudsman news* we have looked at some of the problems that can arise when consumers make payments by cheque and by plastic card. On page 2 of this issue, we take a look at the UK's systems for making regular payments by standing orders and direct debits. We highlight the differences between the two payment systems and provide some recent case studies – illustrating where things can sometimes go wrong.

Over the past year we have seen a small but steady increase in the number of investors referring complaints to us about market value adjustments (MVAs). Also known as 'market value reductions', MVAs, are reductions that firms sometimes make to the value of with-profits investments. On page 10, we outline the types of complaints we are receiving about MVAs, and provide a selection of recent case studies.

Finally, following on from our insurance article last month, on page 8 we provide some case studies illustrating how we have dealt with some of the complaints we have received involving the theft of a car when the keys were left in it, or on it.

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1 banking – standing orders and direct debits

standing order or direct debit?

Many of the complaints we get about regular payments wrongly describe a standing order as a 'direct debit', or a direct debit as a 'standing order'. It's maybe not too surprising that customers get the terms muddled up, because standing orders and direct debits do broadly the same thing, even though they work very differently. It doesn't help, though, when bankers themselves sometimes describe them wrongly.
Here's a brief explanation:

standing orders are customers' instructions to their bank to pay a set amount, to a named beneficiary, at regular intervals (say on the 1st of the month) – *either* for a specific period of time *or* until cancelled.

direct debits are:

- customers' authority for beneficiaries to claim payments (variable in amount and frequency) from the customers' accounts; *and*
- customers' instructions to their bank to allow the taking of those payments.

... a standing order requires the customer's bank to *send* the money.

A standing order requires the customer's bank to *send* the money. A direct debit requires the beneficiary to *claim* the money.

Typically, a standing order might be used to pay a fixed amount to a savings account or to a local club. A direct debit is more likely to be used to make payments that can vary from time to time – such as mortgage instalments or utility bills.

The day-to-day advantage of a direct debit over a standing order is that, as and when the payment amount changes, the beneficiary will claim the new amount automatically – after telling the customer of the change. With a standing order, customers need to give their bank new instructions each time a change is needed.

how the systems work

Standing orders can be simpler than direct debits – mainly because the beneficiary is not involved in claiming payments. At set times, the customer's bank just sends the money to the beneficiary's bank and only the customer can alter the payments.
The beneficiary can be anyone.

In contrast, the variable nature of direct debits means that beneficiaries can claim different amounts at different times. This flexibility is the main advantage of the direct debit system – but there is a potential riskthat unscrupulous or inefficient beneficiaries might claim money that is not due to them.

... a direct debit requires the beneficiary to *claim* the money.

To combat this – and to reassure customers – the direct debit system contains two main safeguards:

- The *direct debit guarantee* provides for the customer's bank to refund disputed payments without question, pending further investigation. (For fuller information about the direct debit guarantee, see the April 2003 edition of *ombudsman news*).
- Direct debits can only be set up for payments to beneficiaries that are approved 'originators' of direct debits. In order to be approved, these beneficiaries are subjected to careful vetting procedures – and, once approved, they are required to give indemnity guarantees through their banks.

Usually, the customer has to sign a direct debit form, although some particularly trusted originators are authorised to set up direct debits where the customer has given authority over the phone. If that sounds a little risky, remember that the originator must have obtained the bank account details from the customer – and that the customer is protected by the *direct debit guarantee*.

Payments themselves are made by a system that is in some ways based on the cheque clearing system. This means that the process usually starts two working days before the money is due to reach the beneficiary's bank account.

Direct debits are processed through BACS (Bankers' Automated Clearing Services), as follows:

Day 1:	BACS receives electronic details of all direct debit payments due on Day 3
Day 2:	BACS sorts the information between banks and gives each bank a report of all payments due on Day 3
Day 3:	Payments are made – the beneficiary's bank account is credited, and the customer's bank is debited

Just as with a cheque, a bank can 'bounce' a standing order or a direct debit if there's not enough money in the customer's account on Day 3 to cover it. And, in most circumstances, the customer can cancel, or 'stop', a standing order or a direct debit up to and during Day 3 – the day of payment.

... standing orders have seen something of a renaissance in recent years.

recent trends and developments

Consumers are making more and more use of standing orders and direct debits. Over the past couple of years, transaction numbers have gone up by about 12%. In fact, standing orders have seen something of a renaissance in recent years – with the increased use of internet banking making it easier not just to set them up, but also to keep them up-to-date.

Since late 2003, BACS has comprised two organisations:

- *BACS Limited* – responsible for physically processing payments, and maintaining the payment network; *and*
- *BACS Payment Systems Limited* – governing the rules under which payments are made, and responsible for maintaining and developing the integrity of payment schemes.

It's still too early to tell what effect this division of responsibility will have. But last year saw the beginning of a major upgrade to the system used to make payments – from telecoms-based to internet-based. This is due to be fully operational by 2005.

The principal advantage of an automated 'regular payments' system is that, if it all works correctly, the right payments are made at the right times without regular human intervention. But ironically, this is also its biggest potential weakness. If, at the outset, payment information is keyed wrongly into the bank's system, then payments will be made wrongly and will continue to be made wrongly until someone spots the mistake. Often, it will be the customer, not the bank, who discovers the problem – maybe many months afterwards, and sometimes only once the person who was expecting the money has complained that they've not received it.

case studies – banking – standing orders and direct debits

■ **38/1**

standing order – whether bank responsible for missing payments after failing to change details of account number and then allocating account number to a different customer

When Miss V came to the UK for a one-year post-graduate course, she rented a property close to the university. At the request of her landlord, Mr J, she opened a bank account at the branch where he had his account. Miss V set up a standing order from this new account to pay her monthly rent of £800 into Mr J's account.

Almost a year later, just before Miss V's course finished, Mr J contacted her to complain that she was behind with the rent. Miss V was certain that couldn't be right. She made a point of checking her bank statements every month and knew that all the payments had been made. But Mr J was adamant – so Miss V got in touch with the bank to try to find out what had happened.

The bank confirmed what Miss V already knew; the payments had all been properly made from her account. Miss V went back to Mr J with that information. Mr J finally accepted her story, but he then complained to the bank, because he had never received the payments in question.

The bank's investigation revealed that Mr J had transferred his bankaccounts offshore shortly after Miss V set up the standing order. It was the bank that had suggested he should do this. Mr J was not resident in the UK but had about 50 properties in the UK that he let out. Most of his tenants – like Miss V – had set up accounts with the same bank. And as part of the process of transferring Mr J's accounts offshore, the bank had agreed to alter all the tenants' standing orders so that their rent was paid into one of Mr J's new offshore accounts. Unfortunately, however, it overlooked Miss V's standing order.

The problem was compounded because, within a few weeks of transferring Mr J's accounts offshore, the bank reallocated one of his old account numbers to another customer. This customer had received Miss V's rent payments for nine months, without querying the payments, and had then withdrawn all the money and closed the account.

Mr J asked the bank to pay him a total of £15,000 – comprising the lost rent of £7,200, plus a significant amount for '*distress and acute embarrassment of loss of face with my tenant*.'

But the bank offered Mr J only £1,600 – the equivalent of the first two months' rent. It said that, as an experienced landlord, he should have spotted much sooner than he did that he was not getting the rent payments. Dissatisfied with this offer, Mr J brought his complaint to us.

complaint settled

Mr J had not been under any legal obligation to check his bank statements. However, we concluded that he might reasonably have spotted the mistake at an earlier stage. The rent from his properties appeared to be Mr J's main source of income, and although he was not resident in the UK, he made frequent visits and looked after the properties himself – rather than using a managing agent.

It took quite a few phone calls, but we managed to mediate a settlement whereby the bank paid Mr J a sum equivalent to half of the missing rent (£3,600), rounded up to £4,000 to cover lost interest and to provide some allowance for the inconvenience he had experienced.

... we managed to mediate a settlement.

We later found out from the bankthat it had also received a complaint from Miss V for '*distress and acute embarrassment of loss of face with my landlord*'. That dispute was not referred to us, as Miss V accepted the bank's offer of £200 in settlement, somewhat less than the £5,000 she had originally asked for.

■ **38/2**
standing order – customer intends to make only 10 monthly payments and complains after bank has made 13 payments – bank says it followed her instruction to pay 'until further notice'

A teacher, Mrs B, agreed to buy a car from her colleague, Mr M, for a total of £4,000. She gave him £3,000 in cash and arranged to pay the rest of what she owed him in 10 monthly payments of £100. She set up a standing order with her bank to make the payments to Mr M's account.

It was only after the bank had made 13 monthly payments into Mr M's account that Mrs B realised that there was a problem. By that time, she'd fallen out with Mr M, because the car had proved troublesome and costly to repair and she didn't think it had been worth what she'd agreed to pay for it. She asked Mr M to pay her back the extra £300 but he refused.

... the bank denied that it had done anything wrong.

Mrs B then complained to her bank. She asked it to refund the three payments that she said it had made in error. The bank denied that it had done anything wrong and it rejected her complaint.

It told Mrs B that it had known nothing of the underlying transaction, so had no reason to suspect anything might be amiss. It said it had simply followed her instructions, and it showed her the standing order form she had completed and signed. This said '*pay Mr M £100 a month*', and she had ticked the option indicating that payments should continue '*until further notice*'.

complaint rejected

When she referred the complaint to us, Mrs B maintained that, because she knew nothing about standing orders, she'd relied on the bank to help her fill in the form. But her bank statements made it clear that she'd set up standing orders before, and there was nothing to show that she'd asked the bank for any help before filling in the form in question. We concluded that she had probably simply made a mistake when filling in the form and was now trying to blame the bank for her own error. We did not uphold her complaint.

■ 38/3

direct debit – bank Y takes direct debit payments from customer's account with bank A – bank Y ignores repeated reminders that it is taking the money from the wrong account – customer's repayments go into arrears

Mrs G had two current accounts with bank A. She took out a loan with a different bank – bank Y – and arranged to repay it by direct debit payments from her 'number 1 account' with bank A.

To begin with, all went according to plan. But a few months later, Mrs G moved house. She said she wrote to both banks, telling them her new address, and asking that all future loan repayments should come from her 'number 2 account' with bank A. At the time, she believed both banks had received her letter, but bank Y later said that it had never seen it.

When bank Y claimed the next loan repayment, bank A spotted that it had mistakenly claimed the money from Mrs G's number 1 account. Bank A made sure the repayment was taken from the number 2 account, and it wrote to bank Y to remind it of Mrs G's recent instruction.

However, bank Y ignored the letter from bank A and, for the next six months, it continued to claim payments from Mrs G's number 1 account. Every month, bank A corrected the payments, and it kept on asking bank Y to sort matters out at its end.

On the seventh occasion, bank A failed to intervene to ensure that the loan repayment was debited to the number 2 account. And, because Mrs G did not have enough money in her number 1 account to cover the repayment, it was not paid. So Mrs G's loan fell into arrears.

Bank Y wrote to Mrs G about the missed payment. However, it sent the letter to her old address, so she never received it. The problem did not come to light until after bank Y had registered the defaulted loan with the credit reference agencies.

Mrs G then complained to both banks. Bank A, which had tried to help throughout but had overlooked sorting out the seventh wrongly-claimed payment, accepted responsibility for that failure and offered Mrs G £200 in compensation.

But bank Y maintained that it had done nothing wrong. It said it had not known that she had wanted to change her instructions, or that she had moved house. Mrs G then referred her complaint to us.

complaint upheld

When we looked into what had happened, we said that bank A had not been under a primary obligation to keep on sorting out bank Y's mistakes. We told Mrs G that its offer of compensation was generous, and that she should accept it.

However, we thought that bank Y's conduct had been far from satisfactory. Even if it had not received Mrs G's original letter, it was stretching credibility too far for it to say that it had not received any of bank A's repeated reminders.

So, provided that Mrs G made up the missing loan repayments (which she was happy to do), we told bank Y to:

- refund all charges and the additional interest it had levied on the loan;
- make sure the adverse credit reference agency entries were removed; *and*
- pay Mrs G £400 compensation for the distress and inconvenience caused by its repeated errors.

Bank Y reluctantly agreed. But then it mistakenly paid her the £400 twice – once to her number 1 account and once to her number 2 account. It was Mrs G who spotted the double payment, not the bank. She asked if it wanted the surplus £400 back – but by that stage, it seemed that bank Y was rather embarrassed by the whole affair, so it told her she could keep it.

38/4
direct debit – when customer complains, bank causes confusion by telling him the direct debit is a standing order

Mr K was the treasurer of a small charity. He set up a direct debit to pay the service charge for the charity's office premises. The annual amount was £376.49, payable quarterly in advance by means of three payments of £94.12, and one of £94.13.

A few months later, after the landlord had claimed the higher payment as the first of the quarterly instalments, Mr K complained to the bank. He said he had expected the higher payment to be claimed last, and that '*although the variation is only 1p, it is nonetheless of considerable inconvenience to me because of book-keeping corrections.*'

It later became clear that the landlord had explained to the charity exactly what payments would be taken when. So the bank had not done anything wrong.

However, in trying to deal with the complaint, the bank told Mr K that the payment instruction was a standing order (*not* a direct debit) and that the fault was all his. It took the bank three attempts, and as many weeks, to give Mr K a reasonable explanation – which, because of the earlier confusion, he then either didn't understand or didn't accept.

complaint rejected

After we got involved, we spent some time explaining the system to Mr K. But we also told the bank that because of its basic misunderstanding at the outset, and its ineptitude in trying to deal with such a simple matter, it should pay the charity some compensation. It agreed to do so.

2 insurance case studies – keys left in or on cars: a continuing problem

In the last issue of *ombudsman news* (issue 37, May/June 2004) we set out some of the general principles that we take into account when assessing 'keys in car' cases – where motor insurers have rejected claims for theft, or attempted theft, because the ignition keys were left in – or on – the vehicle.

As we explained, although practically all motor insurance policies include a clause excluding claims in these circumstances, insurers still need to draw the attention of policyholders to this clause, as it constitutes a major restriction on the scope of cover. Where insurers fail to do this, we may uphold a complaint, even though the circumstances of the theft fall within the scope of the exclusion clause. In such a case, we still consider whether the policyholder was in breach of any 'reasonable care' condition in their policy – that is, whether they acted 'recklessly'. If we are satisfied that they did *not* act recklessly, we will require the firm to meet the claim.

The following case studies illustrate how we put these general principles into practice. It is important to emphasise that we decide each case on individual facts; none of the following represents a precedent for future cases.

... insurers need to draw the attention of policyholders to this clause.

- **38/5**
  car stolen from driveway – whether firm was right to reject complaint on the grounds of customer's 'carelessness'

Miss L's car was stolen from the driveway of her home while she was inside the house. She neither saw nor heard the theft. When she put in a claim to the firm, it asked her to send it her car keys. However, she was only able to produce the spare ignition key.

Taking this as evidence that the key had been in (or on) the car when it was stolen, the firm rejected Miss L's claim. It said that by failing to '*exercise reasonable care in safeguarding her car*' she had breached a general condition of her policy.

Miss L objected to this. She said that the key had definitely not been in the car when it was stolen. She had lost the key a month earlier and had been using the spare. She was adamant that she had not been '*careless*', as the firm had suggested. After the firm rejected her complaint, she came to us.

complaint rejected

We agreed with Miss L that she had not been '*reckless*'. As we noted in our last issue, someone is reckless if they recognise a risk, but deliberately '*court*' it. Miss L had not done this, so the firm was wrong to say that she had breached the 'reasonable care' condition.

... Mr A had been prejudiced by the firm's failure to highlight the clause.

However, the firm's policy also contained a specific (and very comprehensive) clause that excluded claims for cars stolen when the keys were left in them. The firm had specifically highlighted this clause when it sold Miss L the policy. And as we were not satisfied with Miss L's explanation that she had lost the original car key, we concluded on balance that it was likely that she *had* left the key in, or on, the car.

We were satisfied that the circumstances of this theft did fall within the scope of that exclusion. She could be said to have '*left*' the keys in the car because she had gone into the house, and was too far from the car to be able to prevent it being stolen. In addition, the fact that the car was parked so close to the road meant it was relatively vulnerable to an opportunistic thief. We therefore rejected the complaint.

■ 38/6
keys left in ignition – firm rejects claim – whether firm had highlighted exclusion clause

Mr A parked his car opposite a letterbox and jumped out to post a letter, leaving the key in the ignition. While he was crossing the road to reach the letterbox, someone stole his car.

Mr A was horrified when the firm rejected his subsequent claim on the grounds of its 'keys in car' exclusion clause. He said that the firm had never told him the policy included such a clause and, eventually, he complained to us.

complaint upheld

By turning his back on the car and walking away from it, Mr A had fallen foul of the '*keys in car*' clause in the policy. In legal terms, he had left the car '*unattended*' – in other words he was not close enough to the car to make prevention of the theft likely, as established in *Starfire Diamond Rings Ltd v Angel*, (reported in 1962 in Volume 3 of the *Lloyd's Law Reports* page 217); and in *Hayward v Norwich Union Insurance Ltd*, (reported in 2001 in the *Road Traffic Reports*, page 530).

Mr A accepted that he *had* left the car unattended. But he claimed that none of the policy documents that the firm had sent him (such as the policy schedule and certificate) referred to the '*keys in car*' exclusion. The firm had set out the exclusion in the policy booklet, but it had done nothing to draw Mr A's attention to it when it sold him the policy, as it should have done in accordance with industry guidelines.
We therefore felt it was fair and reasonable to assume that Mr A had been prejudiced by the firm's failure to highlight the clause.
If the firm had clearly referred to the clause on the policy certificate or schedule, Mr A might well have acted differently.

And we were satisfied that Mr A had not acted '*recklessly*'. Applying the test of '*recklessness*' as set out in *Sofi v Prudential Assurance* (1993) – he had not even recognised that there *was* a risk, let alone deliberately courted it. We therefore required the firm to pay Mr A's claim.

■ **38/7**
key left in car – theft recorded on CCTV – whether firm right to use 'key in car' exclusion to refuse claim

Mr H drove to the council-run tip to get rid of an old carpet. While he was disposing of the carpet, someone stole his car. He had left the keys in the ignition and, although he hadn't walked far from the car, he did not hear or see anything suspicious. He only realised that his car was gone when he turned back towards where he had left it.

The firm turned down Mr H's claim because he had left his keys in the car. When it rejected his complaint about this, Mr H came to us.

complaint rejected
The firm had based its decision not to pay the claim on CCTV footage that it obtained from the council. This showed Mr H walking away from his car with the carpet. It also appeared that he had left the car's engine running.

We agreed that the firm had been correct in turning down the claim on the grounds of its 'keys in car' exclusion. Mr H had turned his back on the car after leaving it in a public place and he was completely oblivious to the theft until after it had happened. He had walked a fair way from his car, so he was unlikely to have been able to prevent the theft.

In this instance, Mr H had no excuse for not being aware of the policy exclusion. The firm had highlighted it very clearly on the policy certificate, a document that every motorist is required to have by law. We therefore rejected his complaint.

3 investment – market value adjustments

Market value adjustments (MVAs) generally take the form of a charge levied on investors who withdraw some, or all, of their money from a with-profits policy before the policy has reached the end of its term. MVAs are applied as a percentage of the amount that the investor withdraws. So, for example, if a firm decides to make a 15% MVA, then when an investor cashes in an investment worth £10,000, the investor will receive £8,500.

The use of MVAs has become more widespread in the last two or three years, and the size of the percentage that firms charge has grown considerably in that time. In part, at least, this reflects stock market conditions, which have caused a general fall in the value of the funds' underlying investments.

Normally once a year, based partly on how well a with-profits fund has performed over the previous 12 months, a firm will decide whether it will declare a bonus – and what size any bonus should be. Once a bonus has been added to a fund, it cannot usually be removed.

Firms use MVAs to try to ensure that policyholders who cash in some or all of their with-profits investment before the end of the policy term do not disadvantage the remaining policyholders.

In many of the complaints we see, investors say that the firm had never mentioned the possibility of an MVA. It therefore came as a particularly unwelcome surprise to them when they withdrew their money and found that a large percentage had been deducted. We are also seeing complaints from investors who discover, after investing their money, thatthey then have no way of making any withdrawals before the end of the term without the firm imposing an MVA. This can be a particular worry for those who had planned to draw a regular income from their investment.

Some complaints about MVAs also concern, or are influenced by, the general fall in value of bonuses on with-profits policies in recent years, and the fact that smaller bonuses may lead to a reduced level of income from the investment.

In dealing with complaints involving MVAs, we look to see whether the firm's policy documents stated clearly that MVAs might be applied and explained the effect they could have. We also look at the investor's circumstances and requirements at the time of the advice, to see if that advice was appropriate. This will be particularly important if MVAs were being applied at the time of the advice.

In such cases we will look at whether the investor would have had a clear understanding – from the product documents or from the adviser – of the potential impact of an MVA if, for example, the investor needed access to their money in the shorter term.

Where we find that:

- the investment advice was suitable;
- the MVA was correctly applied; *and*
- the policy gave clear information about possible MVAs;

we will not uphold the complaint.

A firm's decisions about when it will apply an MVA and how large it will be, together with its decisions aboutbonuses, are usually matters that are entirely for the firm itself to determine. We would not generally lookinto complaints about these issues, since – under our rules – we can dismiss a complaint without considering its merits if it concerns a firm's legitimate exercise of its commercial judgement.

However, we may uphold a complaint if an investor lost out as a result of being wrongly advised to invest in a with-profits fund, or where a firm failed to give clear information about MVAs in its policy document.

... the use of MVAs has become more widespread.

case studies – market value adjustments

■ **38/8**

pensioner seeking income – advised to invest in with-profits bond – firm reduces bonuses to zero, then tells pensioner it will make an MVA if he withdraws capital

After Mr F retired, he found that his pension only just covered his basic living expenses. He had a modest amount of capital, invested in a high-interest savings account with his bank, and he soon began to rely on the interest from these savings to supplement his income.

Wondering if there was any way in which he could improve on the amount of interest he was getting, Mr F consulted the firm. It advised him to put 60% of his capital in its with-profits bond. A feature of this particular bond was that his capital was guaranteed not to drop below the amount he invested, as long as he did not withdraw more than a pre-set amount. In effect, this meant that he could not receive any more income than the value of the annual with-profit bonuses.

Just over a year after Mr F transferred his money into the bond, the firm reduced its bonus rate to zero. As a result, Mr F was not able to take any income at all.

He contacted the firm to ask why it had not warned him that this could happen, and to say that he wished to cash in his investment and put the money elsewhere. The firm told him that it would apply an MVA, significantly reducing the amount he would get. Mr F then complained that he had not been told that his capital might be reduced in this way. When the firm failed to uphold Mr F's complaint, he came to us.

complaint upheld

We concluded that Mr F had been wrongly advised to invest in this bond. It was not suitable for him, as he was relying on this investment for a steady level of income for the rest of his life and there was always a possibility that the bonus level could drop, perhaps to zero.

The fact that the firm might charge an MVA also made the bond unsuitable. The MVA could effectively lock Mr F into the investment unless he was willing and able to suffer a significant capital loss.

We upheld the complaint and asked the firm to return to Mr F the full amount he had originally invested. We did not award any further sum for 'loss of use' of his money; the amount of income he had withdrawn from the bond was approximately the same as the amount of interest he would have received if he had left the money in his bank account.

■ **38/9**

customer invests in five-year with-profits bond – misunderstands illustration of effect of MVA on early withdrawals and fears value of his bond has dropped

In 2002, Mr T invested £50,000 in a five-year with-profits bond. Two years later, he was shocked to receive a statement from the firm that seemed to suggest his bond was now worth only £40,000. Dissatisfied with the firm's response to his complaint about this, he contacted us.

complaint withdrawn

Mr T could not understand how such a 'loss' had come about, particularly since he had not taken any income from the bond and the firm's representative had not warned him that the value of his investment might fall.

... he had not been told that his capital might be reduced in this way.

After looking at the statement that the firm had sent Mr T, we explained to him that the actual value of his bond had *increased* – it was now £51,000. The firm had quoted the figure of £40,000 to illustrate the amount he would receive if he cashed in his investment at that point, since the firm would apply an MVA to the withdrawal.

We explained to Mr T how MVAs work, and pointed out that his policy provided a guarantee that he would get the full value of the bond after five years, without any reductions. Mr T said he was happy to leave his money invested in the bond for the full five-year term. Satisfied with our explanation and relieved that the value of his bond had not gone down – Mr T told us he did not wish to proceed with his complaint.

■ 38/10
retired couple invest in with-profits bonds for improved level of income – firm cuts bonuses – couple unable to withdraw their capital without deductions

Mr and Mrs A, who were retired, received a very small income from their pensions. However, they were able to supplement this with the interest Mr A received on his fairly substantial savings, spread across several different bank accounts.

After seeking the firm's advice about increasing the level of income available from these savings, Mr A took 90% of his savings out of the bank accounts and put the money in several of the firm's with-profits bonds. For a short time this did produce a slightly higher income. However, it wasn't long before the firm began cutting bonuses.

Mr and Mrs A soon found they were getting only 10% of the income they'd had from the bank savings accounts. Greatly alarmed by this, they decided to withdraw all the money from their bonds as quickly as possible and put it back in the bank accounts. However, when they contacted the firm to arrange this, the couple discovered that MVA deductions would make considerable inroads into the total amount they got back.

Mr A complained that they had never been told there was any possibility that the level of income they got from the bonds could drop. He also said they not been warned that an MVA might apply if they withdrew their funds before the bonds had run their full term. When the firm rejected his complaint, he came to us.

complaint upheld

We upheld the complaint. The couple were dependent on the income from their capital to meet a large proportion of their everyday living expenses. This type of investment was therefore unsuitable for them, particularly since the MVAs meant they could not withdraw their money without losing some of their capital.

We asked the firm to return the full amount that Mr and Mrs A had originally invested in the bonds. We said it should also work out whether it owed them an additional sum for 'loss of use' of the money. It should do this by calculating the amount of interest the couple would have received if they had left their money in the bank accounts, and deducting the amount they had received as income from the bonds up until the point when the couple withdrew their investment.

... the firm's use of MVAs meant that her money was effectively 'locked in'

■ **38/11**
customer invests in five-year with-profits bond – decides to cash it in after three years – claims firm's application of MVA is 'jeopardising her future livelihood'

Ms C, who had been divorced for some years and had no children, made up her mind to resign from her job and move to Spain.

Nearly three years earlier, she had invested £10,000 in a with-profits bond. She had originally intended to leave this money invested for the full five-year term. However, once she began making plans to move abroad, she changed her mind and would decided to cash in the bond. She had worked out that the proceeds of the bond, together with the money she got from selling her flat, would enable her to buy a property in Spain and cover her expenses until she had settled in and found a new job.

When she contacted the firm to cash in the bond, she was greatly dismayed to learn that the firm would apply a MVA, substantially reducing the total amount she got back. She complained vehemently, saying that the firm had no right to reduce the value of her capital in this way, and that it was 'jeopardising her future livelihood'. However, the firm rejected her complaint.

complaint rejected

When she referred the dispute to us, Ms C insisted that the firm had not been entitled to apply the MVA. She insisted that – when she was advised to invest in the bond – she had been told there was no risk to her capital. She also complained that the firm's use of MVAs meant that her money was effectively 'locked in' until the end of the five years. She said that her changed circumstances meant this restriction was not acceptable to her.

We looked first at the firm's policy documents. These stated clearly that the firm was likely to impose an MVA if investors took any of their money out of the bond before the end of the term.

We then looked at what Ms C's circumstances had been when she was advised to make this investment. We found that at that time she had been 40 years old, in full employment, and earning enough to leave her with a significant surplus after she had covered all her living expenses. In addition to the £10,000 she put into the bond, Ms C had over £30,000 of savings in her bank account.

She had told the adviser she had no plans to retire from her job until she was at least 60. And there was nothing to indicate that she might need to withdraw any money from the bond before the policy term was up. This was the first time that Ms C had invested in a with-profits bond. However, on several previous occasions she had left sizeable sums of money – untouched for over five years – in the type of savings accounts that penalised savers heavily for withdrawing any capital before the first five years were up.

We therefore rejected the complaint. The advice to invest in the with-profits bond had been suitable for Ms C's needs at the time of the sale and the firm's literature had given a clear explanation of MVA's.

*working***together**events 2004

mortgage endowment complaints
a conference for smaller firms

Manchester Conference Centre – 29 September 2004

The conference addresses key issues relating to mortgage endowment disputes, including 'suitability' of the sale and the approach to redress.

Aimed specifically at smaller firms, dealing with relatively low numbers of complaints, the conference also provides the opportunity to discuss some of these issues informally with senior staff from the Financial Ombudsman Service.

The conference features:

- presentations by an ombudsman and other senior staff
- discussion groups on key mortgage endowment topics
- buffet lunch
- value for money – just £125 + VAT per delegate.

For more information, look on our website *or* email your details to conferences@financial-ombudsman.org.uk
***or* complete this form and return it to us.**

Please send information about the Manchester *working***together** conference:

name(s)

firm

phone

email

office address

Please send this form (or a photocopy) to: Caroline Wells, Industry Relations Manager
Financial Ombudsman Service, South Quay Plaza, 183 Marsh Wall, London E14 9SR

ask ombudsman news

taped evidence

Q I have been told that you sometimes accept as evidence tape recordings made by consumers – without a firm's knowledge – of telephone conversations with a firm. Surely, unless the firm explicitly consented both to the making of the recording and to the consumer sending it to you, this is unlawful and a breach of firms' rights to privacy?

A Someone commits an offence if they intentionally, and without lawful authority, *intercept* a phone conversation between two other people. But, generally speaking, it is not unlawful for someone to record a phone conversation in their own home, provided they are one of the participants and the recording is for their own use. The legal difficulties tend to arise when recordings are disclosed to third parties.

It does not happen often, but firms as well as consumers will sometimes ask us to consider tape recordings. Under our rules, we have a wide power to admit evidence, and are entitled to exclude or include some types of evidence that would otherwise be admissible, or inadmissible, in a court of law.

We look at each individual case on its own merits, and would need to consider the *fairness* of admitting or excluding the recorded evidence supplied by one of the parties to a dispute. In deciding this, we would look at factors such as the relevance of the evidence on tape, how exactly it was obtained, whether it has breached a party's rights of privacy and whether participants were misled into saying something they would not otherwise have said. Similar considerations apply to video-recorded evidence.

In any case where we decided to admit recorded evidence, we would obviously give the other party a fair chance to consider and respond to the evidence before we reached any conclusions.

time-limit changes

Q I think I saw somewhere that there are new time limits within which complaints have to be brought to the Financial Ombudsman Service. Is that so – and what are these time limits?

A On 1 June 2004, the FSA made changes that will affect the time limits within which customers can make mortgage endowment complaints to firms, and refer them to the ombudsman service. The changes apply *only* to mortgage endowment complaints that are not already time limited under the old rules. Complaints about matters other than mortgage endowments are unaffected by the changes.

In essence, firms will in future have to send the relevant customers written notice of a final date for making a complaint. Further information is available from the FSA website (www.fsa.gov.uk). In a future edition of *ombudsman news*, we will give more details about the new rules, and about the transitional arrangements for mortgage endowment complaints that are already 'in the system'.