complaint

Mrs G has complained that advice she received from CIS Unit Managers Limited ("the business") in 2001 to pay a regular contribution of £100 per month to each of three investment funds of an Individual Savings Account (ISA) for capital growth was unsuitable for her. She is represented in her complaint by a third party adviser.

Specifically, her representative has said that:

- Mrs G was an inexperienced, first -time investor with deposit-based savings and was wholly reliant on the adviser for financial advice;
- At the time, she was retired with no major financial liabilities. Her husband (henceforth referred to as "Mr G") was one year from retirement;
- Her attitude to investment of 'balanced' did not match her personal and financial circumstances;
- While she held an endowment policy that had just matured, this did not give her an insight into the nature of an equity-based investment;
- Other, more suitable products, such as cash ISAs, were not discussed;
- At the point of sale, the couple's net disposable income was modest and the monthly contribution to the investment came partly from the proceeds of her maturing endowment policy and partly from capital savings;
- Given Mr G was shortly due to retire, no assessment appears to have been made regarding their ability to continue funding this investment in retirement.

background

Mrs G's complaint was investigated by one of our adjudicators, who concluded that it should be upheld because he considered that the advice was not suitable or affordable for her in her circumstances at the time.

The adjudicator specifically noted that she was retired and that Mr and Mrs G's combined disposable income was modest. He doubted that the investment was ever likely to be affordable and, in the event, Mrs G took several capital withdrawals having ceased contributions to the investment after 16 months.

With regard to the risk nature of the investment, the adjudicator felt that, in her circumstances, Mrs G should not have been considered a 'balanced' investor. In deciding whether she had made a financial loss from this investment, comparison should be made between the rate of return she actually received from the ISA and the rate of return she would have received had she placed the funds on deposit earning interest at a rate equivalent to Bank of England base rate.

The adjudicator also noted that the level of Mrs G's income and her savings made it likely that she was a non-taxpayer who could claim back income tax deducted from interest on deposit-based savings.

Therefore, the adjudicator's view was that the comparison should be made between the actual return Mrs G achieved from her investment and gross equivalent of the Bank of England base rate.

In response, her representative welcomed the decision to uphold the complaint but made the following points:

- Mrs G was prepared to take a (small) degree of risk and a comparison between the return she actually received on her contributions and a return calculated at 1% above the Bank of England base rate was more appropriate;
- The contributions to the ISA came from the proceeds of a maturing endowment policy she deposited in an account specifically opened by the adviser to “drip-feed” a monthly contribution to the investment. The adviser contrived a complex process of reinvesting the policy proceeds to maximise their own reward and, in doing so, placed the client’s money at risk. When this maturity value was exhausted Mrs G stopped the contributions;
- At maturity, the ‘best’ option would have been for Mrs G to reinvest in a similar with-profit fund or bond for which she would have received a 2% incentive bonus and lower initial charges;
- Mrs G was historically a ‘cautious’ investor, who should not have considered ‘balanced’ or ‘adventurous’ funds;
- The documentation completed at the point of sale appears to have been completed in haste and the ‘suitability report’ was issued post-sale, which casts doubts on the accuracy of the information and afforded Mrs G little time to consider the advice.
- If the adviser had given the maturity cheque to Mrs G, she could have reinvested some of it in a similar with-profits plan and effected a £25 month ‘top-up’ as they had done with the maturing policy into a “life” ISA. This would have been both affordable and suitable and given the clients the 2% bonus.

In reply, the adjudicator was not inclined to change his view that Mrs G’s circumstances in 2001 required her to adopt a risk-averse approach to savings. In the meantime, he has notified both CIS Unit Managers Limited and Mrs G’s representative that, for redress purposes, a comparison with the return equivalent to Bank of England base rate may not be appropriate, as this return may not necessarily reflect the return Mrs G might have received from deposit-based savings. He believed that using a ‘benchmark’ or ‘index’ incorporating an average return from fixed rate bonds more accurately reflected the return she would receive in determining her financial loss.

Nevertheless, as no agreement has been reached in this complaint in any event, it has been referred to me for review.

my findings

I have considered all the available evidence and arguments from the outset, in order to decide what is fair and reasonable in the circumstances of this complaint. Having done so, I find that I agree with the conclusions reached by the adjudicator, and for essentially the same reasons.

My understanding of Mrs G’s financial circumstances at the point of sale is that she was retired and her total income meant that she appeared to be a non-taxpayer. Her husband was still in receipt of an income from employment, although he was due to retire in around one year’s time on pension income of approximately 40% of his final salary. Even while Mr G was in employment, their total net disposable income was modest. Also, other than the maturity proceeds of the endowment policy, their savings amounted to two small capital sums held on deposit.

Therefore, it is evident that, approximately 12 months after the advice was given, when Mr G's income from employment would cease, Mrs G would then be heavily reliant on her savings to supplement their income.

In these circumstances, I believe an overriding consideration for her was to ensure that her capital remained secure before Mr G retired.

While her attitude to risk was recorded as 'balanced', based on her personal and financial circumstances, I would not accept that Mrs G could be regarded as anything more than a very cautious investor, if she could be considered an investor at all, and one who might be prepared to accept a risk to the growth potential of her capital but not to the original amount invested. Even if she might have been considered a very cautious investor before 2001, in my view, her financial position at the point of sale meant that she could ill-afford to take *any* risk with her investments as she had no means of recouping potential investment losses.

That she ceased contributions to this investment once the proceeds of the maturing endowment policy had been exhausted, and that she has taken several capital withdrawals from it to-date, persuades me that this investment was not likely to continue to be funded for long term capital growth.

I agree with the adjudicator that these investments were inappropriate for Mrs G in her circumstances at the time and that redress should be based on the assumption that she should not have been asked to consider an investment that presented any degree of risk to her capital, let alone the degree of risk represented by the three funds she selected.

fair compensation

In assessing what would be fair compensation, I consider that my aim should be to put Mrs G as close to the position she would probably now be in if she had not been given unsuitable advice.

I agree that Mrs G would have invested differently. It is not possible to say *precisely* what she would have done differently. But I am satisfied that what I set out below is fair and reasonable given her circumstances and objectives when she invested.

To compensate Mrs G fairly, the business must:

compare

- the performance of Mrs G's investment

with

- the position she would now be in if the investment had produced a return matching the average rate for fixed rate bonds with 12 to 17 months maturity as published by the Bank of England

If there is a loss at the date of this decision, the business should pay this to Mrs G.

I have decided on this method of compensation because I consider that Mrs G wanted to achieve a reasonable return without risking any of her capital. She was prepared to invest for a longer period of time, but with some flexibility.

The average rate would be a fair measure given Mrs G's circumstances and objectives. It does not mean that she would have invested only in a fixed rate bond. It is the sort of investment return a consumer could have obtained with no risk to her capital.

how to calculate the compensation?

The compensation payable to Mrs G is the difference between the *fair value* and the *actual value* of her investment. If the *actual value* is greater than the *fair value*, no compensation is payable.

The *actual value* is the value Mrs G will receive if it is surrendered at the date of my decision.

The *fair value* is what the investment would have been worth if it had obtained a return using the method of compensation set out above.

The adjudicator has explained how to arrive at the *fair value* and the business should note that guidance carefully. In summary, to arrive at the *fair value* the business should find out the monthly average rate for fixed rate bonds from the date of investment to the *date of this decision* and apply them to the investment, on an annually compounded basis.

additional capital

Any additional sum that Mrs G paid into the investment should be added to the *fair value* calculation from the point it was actually paid in.

withdrawals and income payments

Any withdrawal or income payment that Mrs G received from the investment should be deducted from the *fair value* calculation at the point it was actually paid so it ceases to accrue any return in the calculation from that point on. If there are a large number of regular payments, to keep calculations simpler, I will accept if the business totals all such payments and deducts that figure at the end instead of periodically deducting them.

decision

My final decision is that I uphold Mrs G's the complaint and I require CIS Unit Managers Limited to pay her the amount calculated as set out above.

If my award is not paid within 28 days of the business receiving notification that Mrs G has accepted my decision, simple interest is to be added to any loss at a rate of 8% simple per annum from the date of my decision to the date of settlement.

If the business considers that it is legally obliged to deduct income tax from this interest award, it must send a tax deduction certificate with the payment. Mrs G may reclaim any tax overpaid from HM Revenue and Customs, if her circumstances permit her to do so.

Kim Davenport
ombudsman