

complaint

Mr and Mrs G accepted financial advice given to them by Barnes Independent Financial Advice (“the business”) in 2009 to reduce the risk they would be taking because of falls in the stock market. However, they say they have suffered heavy losses to their capital and an unacceptable drop in their income as a result of this advice.

background

I issued my provisional decision on this complaint in November 2014. In summary, I was minded to uphold the complaint because the recommendations to Mr and Mrs G were in my view unsuitable. They invested their money in an offshore investment bond with most of this being placed into three different life settlement funds. These funds had since been suspended.

Considering Mr and Mrs G’s circumstances and their moderately cautious risk profile, I believed the overall arrangement recommended to them, which also included a smaller amount invested in equities and cash, represented a higher overall risk than they were willing to take.

To help illustrate why I was of this particular view, I made reference to the financial penalty imposed by the regulator on Norwich and Peterborough Building Society. This was for failing to give its customers suitable advice in relation to the sale of structured life settlement Keydata products. The regulator’s Final Notice gave a helpful summary of the structure and risks of the Keydata bonds.

Essentially, this Final Notice showed that investors could lose money if the insurance companies issuing the insurance contracts defaulted on their obligations, or if the issuer of the bond went into liquidation, or if factors changed which affected the rate at which insurance contracts mature. There was also the possibility that investors could lose money if the traded insurance contracts fell in value, or if certain assets did not mature in a way predicted by the financial model.

Even though the three life settlement funds recommended were all open ended, the Keydata International investment actually invested in the Keydata bonds that had been described in the Final Notice. The other two life settlement funds shared all the same characteristics. Therefore I was satisfied these complex and sophisticated investments represented a significant risk to Mr and Mrs G’s capital and were all unsuitable.

However, I noted that the Keydata International fund had actually invested mainly in a SLS issued bond and this particular bond had been subject to a misappropriation from a third party. I believed the business could be held responsible for the unsuitable advice, but it was not responsible for the misappropriation. I said it was difficult to assess what difference this misappropriation had made to the SLS fund but a court could in my view consider that an intervening force, the misappropriation, caused (at least part of) Mr and Mrs G’s losses.

But I said that this service was not limited to the position a court might reach. It was therefore my view fair compensation should still be awarded for that part of the advice that was ultimately connected to the SLS bond because:

- the nature of the advice the adviser gave was in my view clearly in error;
- its assessment of the needs of Mr and Mrs G and of the suitability of the product were in error and it general paid complete disregard to their interests;
- this was the type of investment that they should not have been in and would not have chosen but for the recommendation, and
- there appeared to be an inherent and significant weakness in the investment model used by Keydata in the second hand investments that were to be purchased by the

fund. Other very similar Keydata products failed largely as a result of factors other than this misappropriation; and what I feel to be a fair outcome to this complaint.

I therefore set out how I believed compensation should be calculated in this case.

Mr and Mrs G thanked me for the provisional decision and had nothing further to add.

The business replied also stating that it had nothing further to say.

my findings

I have reconsidered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint. As neither party has made any further submissions or offered any further evidence for me to consider, my conclusion that the complaint should be upheld because Mr and Mrs G received unsuitable advice remains as set out previously, for the same reasons.

my final decision

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £150,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £150,000, I may recommend the business to pay the balance.

Determination and award: For the reasons explained previously, I uphold the complaint.

My aim is to put Mr and Mrs G in the position they would now have been in but for the poor advice. I am satisfied that they would still have invested the original capital in a way designed to produce a return. As there is no compelling evidence about how the original capital would otherwise have been invested, I consider it fairest to assume:

- With reasonable advice, Mr and Mrs G would have had the original capital intact plus a reasonable rate of return.
- The rate of return on the original capital would have been equivalent to 1% more than Bank of England base rate from time to time compounded yearly.
- The rate of return would have been by capital growth, rather than income, and may be taxable in the consumer's hands as a capital gain.

Therefore, I consider Barnes Independent Financial Advice should pay Mr and Mrs G compensation on the following basis:

- A= the capital invested in the offshore bond, less any amounts paid out by way of withdrawals, distributions of capital or before-tax income;
- B= a return on the amounts from time to time of A, by way of a return of the Bank of England base rate plus 1% per annum, compounded annually from the date of investment until settlement;
- C= the value of any offshore wrapper charges balance currently outstanding on the offshore bond;
- D= any personal money or money taken from other investments used to fund the offshore wrapper charges once these could not be met because the unsuitable investments became illiquid;

E= 8% simple interest on D from the date of payment into the bond to meet the bond wrapper charges;

F= the sum of the encashment values of Mr and Mrs G's investments in the joint offshore bond. The individual values should be assessed to be zero if there is no encashment value at present.

G= $A + B + C + D + E - F$.

My decision is that the business should pay Mr and Mrs G the amount produced by that calculation (that is amount G) up to a maximum of £150,000.

For clarification, A and B above should work as follows. Any sum paid into the investment should be added to the calculation from the point in time when it was actually paid in so it accrues the 'reasonable rate of return' within the calculation from that point on.

Any reduction to the investment (excluding the final encashment payment) should be deducted from the calculation at the point in time when it was actually deducted so it ceases to accrue the 'reasonable rate of return' within the calculation from that point on.

In relation to C: if any fund cannot be encashed, for the purpose of C it should be treated as having a nil value. This is provided Mr and Mrs G agree to the business taking ownership of the offshore bond, if it wishes to. If it is not possible for the business to take ownership, then it may request an undertaking from Mr and Mrs G that they repay to the business any amount they may receive from the illiquid investments in future.

I note that there could be a charges balance currently outstanding on the offshore bond. This is likely to be deducted from any encashment value payable to Mr and Mrs G so will be reflected in the overall redress figure. If however the bond provider does not deduct this from any encashment value payable, then the outstanding charges balance should be added to the compensation figure as in "C" above. This is so Mr and Mrs G are able to repay the outstanding charges balance up to that point.

Further, if there is no present encashment value to the investments, then there will be no realisable value from which to deduct the outstanding charges balance. Therefore, the business should add the outstanding charges balance to the overall compensation figure.

Mr and Mrs G will need to cooperate with the business to enable it to make the necessary calculations and in order for the business to take ownership of the investment if it wants to.

Recommendation: As the amount I consider to be fair compensation may exceed £150,000, I recommend that, in this situation, Barnes Independent Financial Advice pays Mr and Mrs G the balance.

This recommendation is not part of my determination or award. It does not bind the business. Whether Mr and Mrs G can accept my decision and go to court to ask for the balance is uncertain. Mr and Mrs G may want to consider obtaining independent legal advice before deciding whether to accept this decision.

Mr and Mrs G should also read our factsheet "compensation over £150,000", which explains our current award limit. It also explains certain implications of accepting our ombudsmen's decisions. The factsheet can be found in the consumer factsheets section of our online technical resource which can be found by clicking the publications tab.

If the compensatable loss exceeds the limit an ombudsman can award and the business does not adopt the recommendation to pay the award in full, any assignment should only concern itself with any future value or distributions from the investments which are in excess of the full compensatable loss as calculated.

To identify this amount, the business should deduct £150,000 from the compensatable loss. The resulting figure is the amount that the consumers are entitled to receive (e.g. retain) by way of future value and/or distributions. Any value or distributions that might be made over and above this amount may be assigned to the business, if the business decides to take a transfer of the bond and those rights.

If the compensatable loss exceeds £150,000 and the business decides to pay the entire compensatable loss, the business is entitled to take, if it wishes, an assignment of the rights to all future values and distributions of the investments within the bond.

Under the rules of the Financial Ombudsman Service, I am required to ask Mr and Mrs G to accept or reject my decision before 23 January 2015.

Doug Mansell
ombudsman