complaint

Mr W's complaint concerns a recommendation in 2013, by Lift-Financial Ltd (Lift), to invest in a particular Business Property Renovation Allowance (BPRA) project. The BPRA scheme, in general, offered the potential of significant tax benefits to investors. Mr W says Lift's due diligence for the underlying investment – development of a commercial building with prospective tenants and a guarantor for the prospective majority tenant (the development) – was flawed.

Some months after Mr W's investment the bank providing finance for the development became concerned about the prospective majority tenant's guarantor and this stalled the development thereafter. Mr W says Lift's due diligence should have foreseen this. He also says the development was at risk of being disqualified for the BPRA scheme because the building was not completely vacant and it needed to be in order to qualify for the scheme.

background

The development was promoted/arranged by a third party and its information memorandum (IM) was produced by the third party. The IM says the third party disclaimed liability for any reliance on the IM's contents in terms of those deciding to invest in the development. Potential investors were told to get advice in this respect and Mr W took advice from Lift.

In the main Lift's recommendation letter to Mr W in March 2013 said:

- He was a high net worth (HNW) individual who had signed a certificate to the effect and his objective was to reduce his tax liability through a combination of BPRA and Enterprise Investment Scheme (EIS) investments. He already held two EIS investments and had invested in BPRA schemes in the past. He held a moderately cautious risk profile for his pension portfolio but he sought to take a high risk approach with the BPRA investment in return for the potential tax benefits.
- He should invest a deposit of £40,000 in the development and this was projected to give him a potential tax relief of around £44,000.
- The development was the only BPRA investment it was likely to recommend to clients at the time. It had a prospective tenant for about 75% of the building (with its parent company standing as guarantor), the developer planned to occupy about 23% of the building and the remaining 2% was already let. [The suitability letter also noted the need for the development to be "empty" in order to qualify for the BPRA scheme.]
- Mr W should note the summary of BPRA risk warnings within the letter and within the IM (including notice that the investment was an unregulated collective investment scheme (UCIS) and was illiquid) and he could withdraw from the investment prior to completion but not thereafter.
- No guarantees were given with regards to returns from the investment or the potential tax relief or tax treatment of the investment.

As stated above, the development stalled after Mr W's investment. In July 2016 Mr W complained to Lift. He elaborated the same complaint to this service and, in the main, said:

- He knew how BPRA investments worked and expected an experience with the development to mirror his previous experiences in BPRA schemes. At the time the development was recommended, an alternative BPRA scheme was available. He had positive experiences of investing in the alternative scheme twice in 2011 and once in 2012 – they worked as he understood BPRA investments should work. He does not understand why the alternative scheme was not recommended to him, as he expected at the time.

- In March 2013 there was news in a prominent newspaper about HMRC's *major investigation* into BPRA schemes and, in particular, the schemes led by the promoter for the development. Lift told him it wasn't aware of this news and he considers that to be a flaw in its due diligence prior to the investment. Had he been aware of this news he would not have invested in the development.
- Lift told him that the problems with the prospective majority tenant's guarantor became apparent around September 2013 – after his investment. This suggests that no due diligence in this respect was done prior to the investment, had it been done there was information in the public domain that would have highlighted the potential for the problems that later arose. [Evidence of this was presented.] This was another flaw in Lift's due diligence – a significant flaw that led to problems in his investment, as the development stalled when the developer was unable to find a new tenant(s).
- Contrary to the requirements of the BPRA scheme the building was not completely vacant and this led to avoidable costs, within the development, to evict the pre-existing tenants. Lift ought not to have recommended a development that was not vacant and the recommendation letter sent to him did not forewarn him about steps that would be required to obtain vacant possession of the building (eviction of the pre-existing tenants).
- The developer had a history of being involved in failed BPRA schemes. Lift's due diligence was flawed in not identifying this risk prior to the investment.
- The building had a history of failed redevelopments over four years prior to the investment, with three different developers. Lift did not advise him about this.

In his complaint to Lift, Mr W also questioned the suitability of the investment in the context of his moderately cautious risk profile.

Lift did not uphold the complaint. In the main, it said:

- Mr W's moderately cautious risk profile related only to his pension portfolio and, as recorded in the recommendation letter, he agreed to take a high risk approach with the BPRA investment.
- It conducts extensive due diligence on *non-mainstream pooled investments* before recommending them to clients and it has done so for many years. It did the same for Mr W. The development was preferred because it had prospective tenants on standby with a projection of the income to be derived from them – the alternative scheme Mr W referred to was based on potential and uncertain income from hotel revenue and the relevant hotel operator was, in its view, untested. The main problem with the development arose around September 2013 in relation to the prospective majority tenant's guarantor. [In wider correspondence Lift argued that the problem could not have been foreseen because the guarantor was a private equity firm, its accounts were not published in the public domain and were not accessible.]
- It has kept its customers updated on the development since 2013. The individual adviser that made the recommendation to Mr W in 2013 left Lift in December that year. Thereafter, Mr W followed the adviser and transferred his investments to the adviser's new firm. Lift stopped being responsible for updating Mr W after that.
- The BPRA scheme requirements relate to "*qualifying expenditure for the redevelopment*" so Mr W's point about vacant possession is incorrect.
- Given the risk warnings in the recommendation letter and in the IM, and given Mr W's experience it is satisfied that he had full awareness of the risks in the investment. Overall, the investment was suitable for him.

The complaint was referred to this service and one of our adjudicators considered it. She concluded that it should not be upheld. She said Lift was not responsible for the IM, it had undertaken some research into the background of the scheme and had not simply relied on the contents of the IM. She also noted that Mr W had invested in similar schemes before and was aware of the risks involved. His circumstances were such that the advice given was suitable for him at the time. She also noted that Mr W has remained positive about the Lift adviser that recommended the investment to him – to the extent of following him to his new firm. She considered that, on balance, the positive manner in which the adviser has been portrayed, by Mr W, and the longstanding advisory relationship they have suggests that he would have advised him against the investment if he considered it to be unsuitable. [Evidence suggests that Mr W's advisory relationship with the adviser started before 2010.]

Mr W disagreed and elaborated on his complaint points with reference to further evidence about information in the public domain that ought to have featured in Lift's due diligence but did not. He also explained that the adviser did consider the alternative scheme to be more suitable for him and was concerned about the development he invested in, but he was forced to recommend it by the order of Lift's management.

Lift commented further and, in the main, said:

- The exceptionally deep level of due diligence that Mr W suggests was a completely unreasonable expectation at the time of the investment.
- The problem was not with the prospective majority tenant – it was with its foreign parent company that stood as guarantor.
- It was a whole of market firm whose advisers were free to recommend whatever products or solutions they felt suited the requirements of their clients, provided they had done a satisfactory level of research themselves.
- The adviser who sold the scheme did not raise any objections to the panel recommendation for the scheme.

No agreement could be reached so Mr W's complaint was referred to an ombudsman.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

The regulator's rules include "principles" that a regulated firm must follow. One of them is that a firm must conduct its business with due skill, care and diligence. In recent years, the regulator gave guidance on the level of due diligence that is expected of a firm in the context of investment advice. Mr W, following legal advice, has referred to the document containing this guidance and we share the same focus on the following relevant contents:

"***Research and due diligence*** *– we use this expression in this paper to refer to the process carried out by the firm to assess (a) the nature of the investment, (b) its risks and benefits and (c) the provider (to establish whether they believe it appropriate to entrust the provider with client assets). The firm needs to understand these factors in order to judge whether the solution is suitable.*"

"*What constitutes a reasonable level of research and due diligence will differ depending on the adviser's recommendation and the needs of the client. Although the objective of research* *and due diligence is the same across different investments, services and providers, there will be differences in the time and effort taken to achieve it. For example, it will usually take less time to assess a product from a familiar provider investing in familiar assets. Correspondingly it will usually take longer to assess a product from a provider with which the firm is not familiar or which invests in assets the firm has not researched before.*"

"*When firms carry out research and due diligence they should consider whether they can rely on the information supplied by the provider, such as marketing material. Firms can rely on factual information provided by other EEA-regulated firms as part of their research and due diligence process, for example, the asset allocation. However, they should not rely on the provider's opinion, for example, on the investment's risk level*."

Mr W says Lift's due diligence was flawed because, prior to his investment, it was unaware of the negative news in the public domain about the scheme and promoter; because it was unaware of the problems facing the prospective majority tenant's guarantor; because it did not ensure that the building was vacant; because it did not disclose to him the developer's negative development history; and because it did not advise him about the building's negative redevelopment history.

In response to the adjudicator's view, Mr W referred to information he appears to have obtained from the adviser that recommended the scheme when he worked for Lift. I am mindful that he considers the adviser to be credible. He said there was "… *extensive research primarily conducted by* [Lift's Director and the promoter] …" and that Lift's Director "… *personally checked out all the counterparties (via his various sources) to the scheme … and was adamant that this scheme was in the best interests of the firm and all its clients."*

This evidence was presented to support Mr W's assertion that the adviser was forced, against his better judgment, to recommend the development to him. My consideration in this respect is as follows:

- Lift denies the assertion. If the assertion is true then the adviser, who Mr W trusts, misled him in 2013 – even if the argument is that he was forced to do so, it would remain that he did so. If the assertion is not true, then perhaps the adviser is misleading Mr W at present. Either way, there appears to be conflict within Mr W's complaint whereby he says Lift is responsible for unsuitable investment advice but he also says the individual adviser who delivered the advice should not be blamed for the advice or for either misleading him at the time or, perhaps, for misleading him presently. Mr W invited us to verify his account of what the adviser told him by contacting the adviser directly. It is not clear if this was (or was not) done, however I do not consider it necessary. On balance, I accept the accuracy of Mr W's account of what the adviser told him, the question is whether (or not) what the adviser told him is true.

- On balance, I am prepared to accept the internal due diligence process as described by the adviser. Evidence suggests that he had no role in the process because Lift's Director conducted it. Without a role (or interest) in the process I do not consider that he would have any motive to misrepresent it. However, he has an interest in terms of responsibility for the advice given to Mr W. He gave that advice. I do not have enough evidence to conclude that, as he claims, he was forced to advise Mr W against his better judgment. Lift denies the claim, so that means I do not have enough evidence to doubt its denial.

Whilst I am not persuaded that the adviser's evidence helps Mr W's assertion, as I have addressed above, I am however persuaded that it supports Lift's insistence that it researched the project extensively. The adviser was a witness to Lift's Director doing this alongside the scheme's promoter. According to Mr W, the adviser was also a witness to Lift's Director researching beyond the particular project. He said the adviser told him that Lift's Director "… *completed a full and thorough review* *<u>of all the BPRA schemes</u>* *that were available on the market* …" [my emphasis]

On the face of it and without going into details (of Mr W's points) yet, Lift discharged its due diligence duty and the adviser appears to have been a witness to that. The argument might be that another scheme would have been *more suitable* for Mr W. However, that is not the issue to consider. A firm's basic responsibility is to give suitable investment advice – not to give *more* or *the most* suitable investment advice. This also applies to Mr W's reference to an alternative scheme that he considers would have been better for him in 2013. He was an HNW investor prepared to take a high risk approach with a BPRA investment and Lift was entitled to recommend any project that matched his profile and objective.

In terms of the details of what Lift did not do, according to Mr W, I will refer to the regulator's guidance where necessary. In doing so, I address his main points as follows:

- News about HMRC's investigation into BPRA schemes and the promoter in March 2013.

  Mr W's complaint is not about being invested in a BPRA scheme, it is about the specific scheme that was recommended to him. His complaint is also not about problems caused by the promoter, it is mainly about problems caused by the guarantor for the prospective majority tenant which he says Lift ought reasonably to have foreseen. I do not consider his point about this news to be relevant to his complaint. Even if it was, the IM produced by the promoter contained a disclaimer that said the contents should not be relied upon in terms of making investment decisions. It also contained no guarantee about tax treatment – as echoed in Lift's recommendation letter. As such, Mr W knew from the outset that the promoter's representations were not completely reliable and that the same applied to the potential tax benefits. Furthermore, as the regulator's guidance suggests, less due diligence on an investment could be reasonable in relation to a familiar product from a familiar provider. Lift was familiar with BPRA projects (and had done past research into them) and the promoter was a prominent firm in the industry.

- Vacant possession of the building.

  I consider that Lift misdirected itself when it told Mr W, in its 2016 complaint response letter, that vacant possession was not a requirement to qualify for the BPRA scheme. It clearly was a requirement and that was reflected in Lift's recommendation letter in 2013. Nevertheless, I do not accept Mr W's argument in this respect. The recommendation letter informed him that the building was not completely vacant – as I said above, about 2% of the building was already let – whilst also telling him that empty possession was required by the scheme. He ought reasonably to have concluded that a part of the process to follow would be the task of obtaining vacant possession of the minority units that were tenanted. He also ought reasonably to have expected that a part of the project's budget could be used for this purpose. As it appears, it remained possible for the project to qualify for the scheme once the building obtained complete vacant possession.

- Due diligence on the prospective majority tenant's guarantor.

  It is worth being mindful of what the project was. It was a building redevelopment project that involved investors (and their advisers in the background), a promoter/arranger, a developer, a project manager, a construction contractor and finance from a bank. These were the key players and were those who I consider to have been the main counterparties of the project. The majority tenant and its guarantor were prospective. I appreciate they were mentioned in the IM and there appears to be no dispute that due diligence was conducted on the tenant – and some due diligence on the guarantor – albeit not to the standard Mr W expected. However, in simple terms, they were on standby. I am not persuaded that they can be regarded as counterparties of the same level as the key players.

  Mr W should be commended for the research evidence he shared with this service. I accept his point that if he could discover so much about the prospective tenant's guarantor, Lift *could* have done the same in 2013 – as the information was available at the time. I also accept that Lift was obliged to extend its due diligence to the prospective tenant – which it appears to have done – and there is no suggestion that this was flawed. The question is whether Lift *should* have done an extensive level of research on the guarantor – which is where Mr W says Lift's advice was flawed.

  Mr W was not investing in the prospective majority tenant and he was not investing in its guarantor. I have noted the checklist he presented as the minimum that Lift should have verified about both parties but that must be tempered by the fact that he was not putting his money into them. Neither of the parties were "guaranteed" to be in the future of the project – they were expected to be and steps had been taken to facilitate that (such as the terms that were negotiated for the future lease agreement), but as I said above they were not counterparties of the same level as the key players. I consider that Lift's due diligence on the prospective tenant was reasonable to do, however I am not convinced that it was obliged to conduct the extensive sort of due diligence described by Mr W in relation to its guarantor.

  It is not uncommon for development projects to face *bumps* in the process whereby a new tenant(s) is required in order to progress it. I do not consider it necessary to go into the details of events after Mr W's investment – because the focus should be on what Lift did or did not do prior and up to advising Mr W – but it is worth noting that a new prospective tenant was briefly found. Unfortunately that did not work out and the project remained stalled, but if it worked out it is arguable that the project could have progressed. The point that I am noting is that the idea of tenancy for the project always had a degree of uncertainty, until the tenants were put in place; this was part of the risks that Mr W took; it was a risk that ought to have been addressed by Lift's advice and due diligence on the initial prospective majority tenant and there appears to be no suggestion that it did anything wrong in that respect; but I do not consider that Lift was also obliged to conduct extensive due diligence on the guarantor.

  The developer's due diligence, from April 2013 onward, appears to have been the source of concerns about the guarantor that led to the problems thereafter. It appears to have been conducted for the benefit of the financing bank. The suggestion is that if the developer's due diligence identified such concerns Lift's due diligence ought to have done the same. On balance, I am not persuaded enough to agree. As the regulator's guidance suggests, differences in the conduct of due diligence can reasonably exist, depending on the circumstances. The developer had a somewhat primary obligation to deliver the project. In this context, it is possible that it took extra steps to research the prospective majority tenant and its guarantor. Earlier above, I already accepted that Lift *could* have taken the sort of steps Mr W has referred to and the same applies with reference to the steps the developer appears to have taken – but, for the reasons I have given, I do not accept that it *should* have.

- The developer's negative development history and the building's negative development history.

  I have not seen enough evidence to suggest that either of these issues caused a problem(s) in the project, in the context of Mr W's complaint, so I do not consider them relevant to his core due diligence argument. It is arguably implicit that a commercial property in need of redevelopment would have some form of negative history behind it – the need for "redevelopment" would be unlikely if it did not. The purpose of the BPRA scheme was to focus on properties in distressed areas of the country – hence the potential tax benefits as incentives for investors. The potential for the building's negative history was to be expected and ought reasonably to have been expected by Mr W, especially in light of his previous experience in BPRA investments.

Overall and on balance, I am not persuaded that Lift's due diligence was flawed as Mr W has argued.

my final decision

For the reasons given above, I do not uphold this complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 13 April 2018.

Roy Kuku
ombudsman