

complaint

Mr D has complained about the advice he received from Ashley Law Limited ("the IFA") to invest in a Keydata investment. Mr D says the investment was unsuitable for him, particularly in view of the associated risks.

background

In 2005, Mr D invested in the Keydata secure income plan. The product provider, Keydata Investment Services Limited (Keydata), acted as Mr D's agent and purchased the plan. The issuer of the plan was SLS Capital SA ('SLS'), which was a Luxembourg based special purpose vehicle. Keydata went into administration on 8 June 2009 and defaulted on 13 November 2009. Mr D has approached the Financial Services Compensation Scheme (FSCS) for compensation but his claim was rejected.

Our adjudicator recommended the complaint be upheld. In summary, he identified the IFA had a responsibility to ensure any recommendation made was suitable for Mr D's circumstances and requirements. Rather than simply relying on the headline description of the investment, he said the IFA should have been exercising professional judgement about its inherent nature to assess its suitability for his needs. Based on the information that was available at the time of sale, he felt a financial professional should have been able to identify the Keydata investment included a number of significant distinctive features and risks. And that these features and risks meant it was not a suitable recommendation for Mr D, principally because it exposed his capital to a greater degree of risk than he was willing to accept.

But for the unsuitable advice, the adjudicator concluded Mr D would not have invested in Keydata and proposed a method of calculating compensation designed to return him to the financial position he would now be in if he had invested in a way that was consistent with his requirements.

The IFA disagreed with the adjudicator's conclusions, raising the following key points:

- It believes the adjudicator's assessment was based on hindsight. At the time of the sale in 2005, Keydata had a good track record and the IFA could not have been expected to foresee the problems, including the misappropriation in the fund that followed.
- Appropriate risk warnings were contained in the product literature provided at the time of sale. Mr D was an experienced investor with other asset-backed investments and a property portfolio and would have been capable of understanding these documents. As well as his own investments, he also helped arrange ISAs for his family.
- Mr D was not risk-averse as evidenced by his previous investments.
- Based on the information available at the time of sale, the Keydata bond was not a high-risk product and was suitable for Mr D.
- It referred to a media report about another complaint considered by the ombudsman service about the advice to invest in Keydata where compensation was not awarded.

- It does not believe the adjudicator's proposal to add interest to the crystallised loss at the rate of 8% is reasonable, saying this is above the rate payable on low-risk investments during this period.

We have considered complaints about Keydata life settlement funds before and published decisions which set out our general approach to such complaints on our website. The decisions are in the *investment* section of our *online technical resource* which can be found by clicking the *publications* tab.

my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

When considering what is fair and reasonable, I am required to take into account relevant: law and regulations; regulator's rules, guidance and standards, and codes of practice; and, where appropriate, what I consider to have been good industry practice at the time.

I am therefore mindful of the general legal position including: the law relating to negligence, misrepresentation and contract (including the express or implied duty on professional IFAs to give advice with reasonable skill, care and diligence); and the law relating to causation and foreseeability.

The circumstances in which this investment was made are slightly unusual in that the adviser initially recommended another Keydata product, which was withdrawn before Mr D's investment could be finalised. As a result, the sales documentation, including the adviser's report, refers to the initial recommendation. When the original product was withdrawn, Keydata offered alternatives and the secure income plan was selected.

The IFA has previously argued it did not advise Mr D to invest in this specific Keydata product. But it is clear from the evidence provided that the IFA forwarded Mr D's application to Keydata in August 2005 and received commission on the sale. In addition, in his statement following Mr D's complaint, the IFA said he '*advised*' Mr D to invest in the secure income plan. With these points in mind, I am satisfied that Mr D ended up in the Keydata investment because of advice received from the IFA.

As the IFA gave advice about regulated investments, I have taken account of the regulatory regime that applied at the time which includes the relevant FSA principles and rules on how a business should conduct itself.

Taking the relevant considerations into account, it seems to me that the overarching question I need to consider in this case is whether the recommendations given were suitable for Mr D in his particular circumstances. In doing so I need to take into account the nature and complexity of the investments and Mr D's financial circumstances, needs and objectives; understanding and relevant investment experience; and tolerance to investment risk.

The adjudicator has already set out Mr D's circumstances in detail and I agree with his assessment that Mr D was not looking to expose his capital to any significant degree of risk.

In particular, I note the IFA's suitability report states his attitude to investment risk was '*balanced bias towards cautious*', which was described as follows:

... you are prepared to accept a very small degree of risk to try to secure enhanced investment returns.

The adjudicator also set out the risks associated with the Keydata investment and I agree with his assessment that these risks meant it was not suitable for someone only willing to accept a '*very small*' level of risk like Mr D. While I am aware of how the investments were widely viewed at the time, my conclusions are not based on hindsight and I believe it should have been apparent to the IFA at the time that the investments were not suitable for an investor like Mr D who was not willing to expose his capital to a significant degree of risk.

In response to the remaining points raised by the IFA:

It is clear there was a degree of misappropriation within the fund, but the extent to which this impacted on the ultimate failure of the investment is not clear. In saying this, I am conscious that there is limited information about what took place and that other similar Keydata investments, for example those arranged through Lifemark, also failed with no evidence of misappropriation. I will say more about the issue of misappropriation later in this decision.

It does seem clear that Mr D had some investment experience, but I do not believe this somehow discharged the IFA of its responsibility to provide suitable advice. If he had genuinely been a sophisticated investor, I believe it is questionable that he would have required advice at all. Either way, Mr D received advice and the adviser had a responsibility to make sure any recommendation made was suitable. While some of the risks associated with the investment may have been set out in the product literature, the provision of explanatory documentation alone is not sufficient to demonstrate suitable advice was given.

I agree that Mr D was not completely risk-averse. But the adviser did record that he was only willing to accept a '*very small*' degree of risk. In my view, the Keydata investment exposed Mr D's capital to a greater degree of risk than he was prepared to accept.

As stated previously, we have published decisions on other cases involving Keydata investments and it is true that we did not award compensation in one of those cases. But we have awarded compensation in many other cases. Ultimately, I must consider each case on its own merits. This decision relates to Mr D's specific case and it is not appropriate for me to discuss other complaints in this decision other than to say I am aware of previous decisions we have issued and that I am satisfied compensation is merited in this case.

In short, it is my view that the Keydata plan was not suitable for Mr D. The IFA had a responsibility to ensure any advice provided was suitable and, by failing to do so; I consider he acted with complete disregard for his interests. This is not a view reached with hindsight. I have based my findings on the product's suitability for Mr D based on what the IFA at the time of the advice knew or could be expected to find out about the investment and based on reasonable expectations of how the plan would operate.

Having reached the view that the recommended investment was unsuitable, I now need to consider what Mr D would have done 'but for' the advice he received.

I have not seen anything which suggests to me (and I find it highly unlikely) that he would have invested in the plan, if it had not been recommended to him. Nor am I persuaded that

he would have invested in the plan if things had happened as they should. The investment was not suitable for his needs and circumstances, and I do not think he would have invested had he appreciated the risks.

Overall I think it most likely that Mr D would have invested this capital into another investment consistent with his circumstances and attitude to risk. On balance, I consider a fair benchmark to indicate the investment return on his investments is 1% more than the Bank of England base rate compounded yearly from the date of investment until the date the loss crystallised when Keydata defaulted.

fair compensation

As I have concluded that the IFA's recommendation to invest in the Keydata investment plan was not suitable for Mr D, I need to consider what fair compensation should be. Usually I seek to put the investor back in the position they would have been in but for the poor advice.

However, there is a problem with assessing the true value of the investment into the Keydata bond. That is because assets in the bond Mr D invested in were taken and have not been recovered. It is not clear what the inherent value of the SLS investments were before the misappropriation. It is therefore not clear what the relative contributions are, of the underlying investment performance and the misappropriation, to the overall position that there is no value for investors.

So I need to decide whether or not the misappropriation from the Keydata bond produces new circumstances where my normal approach to fair compensation should not apply. It is relevant, therefore, to note the information that is available to me about the circumstances of this Keydata bond and the liquidation of SLS. As I understand the position, the investments made by Mr D were part of the investments held by SLS registered in Luxembourg. Following its liquidation the Luxembourg based liquidator (Baden and Baden) announced that *"at this stage and with all due precaution, it does not appear that there are any remaining assets left"*.

The UK administrator for Keydata explains *"the underlying assets in relation to these plans were liquidated and misappropriated. This means that investors will not receive any income payments or return of their capital, unless recovery actions are successful. SLS Capital is now in liquidation"*.

Following an investigation, the UK Serious Fraud Office (SFO) concluded in April 2011 that *"after extensive consideration we concluded that we had insufficient evidence to secure a prosecution in this case. As a result we decided to focus our efforts on tracing the assets of SLS Capital SA rather than attempting to prosecute. We are continuing to do this"*. In November 2012, the SFO confirmed that despite substantial effort to trace the assets, it has been unable to do so and it was unlikely to do so in the future. As a result, it closed its file.

What precisely occurred between 2005 and 2009 is not clear. However, given the findings of the SFO it seems that there is little (or perhaps more realistically no) hope of any value being recovered from the SLS managed Keydata bonds.

The position, however, is different from that of other Keydata products. The underlying assets associated with other Keydata funds are also seen (at least for the purposes of the Compensation Scheme) as having no value. While the issues with SLS caused significant financial damage to Keydata, I understand that there were also inherent problems with the

investments associated with the other Keydata funds.

There is a further complication. As far as I can ascertain from the information available to me, there is no clear view about the inherent value of the SLS investments before the misappropriation. So it follows that it is difficult to assess the relative contribution of the underlying investment performance on the one hand, and the misappropriation on the other.

My approach to cases such as this is difficult to describe in general terms – much depends on the particular combination of circumstances. But two points can be made:

First, no liability attaches to an adviser who has given satisfactory advice. Second, particular difficulties arise in assessing fair compensation when it seems clear that (as in this case) the customer would not have been in that class of investment at all had it not been for the negligent advice. In such circumstances I might assess fair compensation to be awarded against the provider of the unsuitable advice to put the customer back in the financial position they would have been in but for the poor advice, notwithstanding that such an award may not be made by a court.

But I would need to be persuaded that such an approach represented *'fair compensation'* in the individual case. It seems to me that in assessing what represents fair compensation, I should have regard to the applicable legal principles. But I should also take into account the nature of the advice given and the impact of any award on the parties and reach a view on what I consider to be fair in all the circumstances of the case.

Mr D would not have been in this Keydata product but for the poor advice of the IFA – and he has suffered a significant loss of money. But I also need to be conscious of what is fair to the IFA. The IFA is and should be held to account for the poor advice it gave, but it was not responsible for the misappropriation of the funds, or for the fact that insurance was not in place to cover such an eventuality.

The legal principles of causation and remoteness that might be applied to cases such as this are highly case sensitive and I cannot be definitive about how a court might apply these principles. As such, the most I will be able to consider is what a court is likely to find, when confronted with this particular set of facts.

In my view, a court might consider that the available balance of evidence about the sequence of events reveals that there was an intervening force that caused (at least part of) Mr D's losses: namely the misappropriation. I also think that a court might find that there are no reasonable grounds for suggesting that the IFA could, at the time of sale, have foreseen that the assets underlying the bond might be misappropriated by a third party.

Accordingly a court might conclude that not all of Mr D's losses flowed directly from the unsuitable advice on the part of the IFA. And on this basis a court might not require the IFA to compensate Mr D for all or any of the losses he has incurred notwithstanding the clearly unsuitable advice the IFA gave.

But in assessing fair compensation, I am not limited to the position a court might reach. I think there are other factors in cases such as these, given in particular the specific circumstances of financial investments and advice that I should consider.

In particular, it seems to me that in assessing fair compensation, I should take into account the nature of the advice that has been given. In the present case, I consider that the IFA had a complete disregard for the interests of its clients in giving this advice.

It is frustrating that in the present case the evidence available to me from the relevant authorities here and in Luxembourg is not sufficient to make a wholly reliable assessment of the underlying value of the bonds or the impact the misappropriation had on the value of the investment.

However, in all the circumstances of this case, I cannot lightly ignore the fact that Mr D would not have been exposed to these risks had the IFA carried out its responsibilities properly. Taking all these factors into consideration, I conclude that I should assess fair compensation in this case as putting Mr D back into the position he would have been had he not followed the advice to invest in the Keydata bond. I say this because of:

- the nature of the advice the IFA gave was in my view clearly in error;
- its assessment of the needs of Mr D and of the suitability of the product and it generally paid complete disregard to his interests;
- this was simply a class of investment that he should not have been in and would not have chosen but for the IFA's recommendation;
- the fact that there appears to be an inherent and significant weakness in the investment model used by Keydata. Other very similar Keydata bonds failed largely as a result of factors other than this misappropriation; and
- what I consider to be a fair outcome to this complaint.

Accordingly, I conclude that it would be fair and reasonable to make an award in the particular circumstances of this case – regardless of any arguments about a break in the chain of causation and the remoteness of the loss from the (poor) advice given. Having considered the factors that I have set out in this decision, I reasonably conclude that I should assess fair compensation as putting Mr D back in the position he would have been in, had he not followed the advice to invest in the bond.

I have also considered what award I should make in respect of interest on the crystallised loss. My normal approach is to award 8% simple per year (before tax) on crystallised losses, unless it is clear that another rate would more accurately reflect the costs to the particular consumer for being out of the money concerned.

I have noted the IFA's comments about the rate of interest, but it is important to establish that the 8% figure is not intended to be an interest rate in the way that a bank deposit account pays interest. It is not therefore necessarily intended to reflect what Mr D would have earned from a low-risk investment during this period. Rather it is a rate which I consider to be a fair yardstick for compensating consumers for a wide range of possible losses and lost opportunities they may have incurred.

The consumer might, for example, have:

- borrowed money, or continued to borrow money, at credit card or loan rates which they would not have done if the money had been available to them;
- saved or invested the money in some way producing a variety of possible returns;
- spent the money on holidays, home improvements, or any number of goods which might have given them an unquantifiable return;
- or any combination of these things.

The 8% simple interest rate is gross and is subject to tax – and is a rate often (but not always) used by the courts in not dissimilar situations.

After considering Mr D's particular circumstances, including the total funds recorded as being available to him at the time of sale, I believe being deprived of this money has caused significant financial detriment. As a result, I am satisfied it is appropriate to award an interest rate of 8% per year simple on any investment loss from the date it crystallised until the date compensation is paid.

my final decision

My final decision is that I uphold this complaint. I believe the Keydata plan was unsuitable for Mr D and that Ashley Law Limited acted with complete disregard for his interests.

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation plus any interest and/or costs that I consider appropriate.

My aim is to put Mr D in the position he would now have been in but for the IFA's poor advice. In deciding how to assess fair compensation I consider it fairest to assume;

- with reasonable advice, Mr D 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; and
- the rate of return would have been by capital growth, rather than income, and may be taxable in Mr D's hands as a capital gain.

I consider that fair compensation should be calculated as D, where:

- A = the capital invested in the Keydata plan, less any amounts paid out by way of withdrawals, distributions of capital or before-tax income;
- B = a return on the amount 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 13 November 2009 (when Keydata defaulted and the loss crystallised) or until the date that the last income payment was made if later;

- C = the residual value of the investment that Mr D made in the Keydata plan, which I assess to be zero for this purpose.
- $D = A + B - C$

My decision is that the IFA should pay Mr D the amount produced by this calculation (that is the amount D). To that sum the IFA should add interest from 13 November 2009 (or from the date that the last income payment was made if later) at the rate of 8% per year simple until this award is paid.

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.

I understand that in some cases, consumers have received income payments after Keydata defaulted. It is only fair that such payments are taken into account in my award and I have allowed for this possibility in the award formula.

In relation to C, I understand that the fund cannot be encashed. For that reason, as set out above, for the purpose of C the investment should be treated as having a nil value. However, that is provided Mr D agrees to the IFA taking ownership of the investment if it wishes to. The IFA would then be able to obtain any value of the investment as and when that value can be realised plus any distributions made from it. I would ask Mr D to note that carefully. He will need to co-operate with the IFA to enable it to make the necessary calculations and in order for it to take ownership of the investment if it wants to.

If the IFA considers it is legally obliged to deduct income tax from the interest (ie the amount to be added to part D only), it must provide Mr D with a tax deduction certificate so he can reclaim any overpaid tax from HM Revenue and Customs if he is eligible to do so.

Jim Biles
ombudsman