complaint

Mr B's complaint is that Willow Financial Management LLP's recommendation to transfer his pension fund into a bond with another provider with subsequent investment in an Arch Cru fund in September 2008 was unsuitable.

background

The circumstances surrounding Mr B's complaint was set out in my provisional decision. In summary:

In September 2008 Willow met with Mr B to review his pension and recorded his circumstances in a 'Personal Client Questionnaire' as follows:

- He was 69 years of age, married and retired.
- His attitude to pension planning risk was 'Low'.
- The current value of his income drawdown personal pension was £48,505.
- He had an annuity with another provider giving an annual income of £1,284 plus his state pension of £5,220 a year. He received annual rental income of £11,500.
- He had joint deposit account holdings with his wife totalling £35,000.

Willow's representative produced a recommendation report which included the following:

- Mr B had been using drawdown for a number of years and wished to withdraw as much from the fund as possible in order to get it into his estate.
- The advice was to transfer the funds to a personal pension bond with another provider because Mr B wanted to gain access to the Arch Cru Portfolio fund, but without the costs of setting up a SIPP.
- Mr B's attitude to risk for the monies in question was best described as 'Low to Medium'.
- He should invest 100% of his pension fund into the Arch Cru Portfolio fund, low-to-medium risk.
- Willow was *'happy with a single fund in this instance as it seems a very good fit, and is also a small percentage of your assets. You own several properties, and this therefore represents less than 8% of your estate.'*
- Willow stated that it had talked through how complex the product is, including its heavy reliance on private market investments. It said that Mr B '*understood that the fund's intended behaviour does seem slightly at odds with the internal complexity*' but that the Investment Management Association (IMA) had accepted Cru's view that the fund belongs in the Cautious Managed sector. Willow said that direct enquiries had been made of the IMA and also of Cru's CEO. Willow also quoted from the fund factsheet which said that the target return (exceeding cash returns by 4% pa) cannot be guaranteed and that both the return and the capital is at risk.

In March 2009 Willow wrote to Mr B confirming that dealing in the Arch Cru funds had been suspended by Capita. It said that those people who were drawing income from the Arch Cru funds would need to make temporary arrangements to draw income from other elements of the pension portfolio.

Mr B wrote to Willow saying that the advice to transfer was *'ill-advised'.* Following further correspondence, Mr B made a formal complaint to Willow in January 2010. He stated that he relied entirely on Willow's expertise and that he had since discovered that the fund invested in private equity capital could be described as high risk. He stated that a pension scheme should have a diversified spread of investments, not just one.

I issued my provisional decision in February 2013. I upheld Mr B's complaint. My view was that the recommendation to invest in Arch Cru fund was not suitable for Mr B. In summary I concluded:

- Mr B was a low to medium risk investor seeking a relatively cautious investment and was willing to accept that his withdrawals were likely to deplete his fund over time
- the Arch Cru fund was not a fund suitable for such an investor and this should have been apparent from the information readily available to an experienced financial adviser
- Mr B did not fully appreciate the risks to which his money would be exposed.

Mr B's representative responded, confirming that Mr B had no additional comments.

Willow did not accept my provisional findings and responded in detail. It said, in summary:

- All and any investment changes had been well considered, discussed with Mr B and analysed in detail. Mr B was in property funds whilst they did well and sold his property holdings before the market dipped and was in cash at the start of the financial crisis. Willow had received no recognition for this.
- The transfer to Arch Cru was made after discussion with Mr B and after Willow had carried out considerable due diligence. It was intended to be in the very best interests of Mr B, aimed at protecting value and income. The adviser had acted at all times in Mr B's best interests and is being blamed for the failings of others.
- It was an *'utter disgrace'* that the financial services industry could not see that the fund was mis-managed and mis-priced and that the regulator (then the Financial Services Authority (FSA)) and this service conclude that advisers should have recognised those risks and outcomes.
- The main conclusion was that whatever Willow had done in terms of due diligence and no matter what information about the fund that it had reasonably relied upon, it should have known, given the asset allocation, that the fund was high risk and unsuitable for Mr B.
- Between 2008 and 2009 very few asset classes did not fall dramatically in value. Mr B had lost money and Willow did not disagree that he should be repaid but asking the adviser to redress him, using hindsight and retrospective conclusions, was avoiding where the blame really lies.
- Willow agreed that private equity investment on its own is a high risk investment, but having fully understood the fund manager's approach, the diversification away from public markets meant the fund's behaviour would be much more controlled which is how the fund performed in 2008 during '*calamitous*' market conditions.
- This was a regulated fund, '*signed off*' as suitable by the FSA.
- The IMA had placed it into the cautious managed sector.
- Capita was responsible as authorised corporate director (ACD) for fund pricing.
- The logical conclusion is that there is not a single regulated fund that advisers can trust and if any ever fall in value due to poor investment decisions then the adviser will be at fault and liable to make good an investor's losses.

- The Capita offer amounts to approximately 15% of the original capital value, with 85% being left to advisers who then take ownership of the distressed fund.
- A correctly managed private equity fund would have recovered by now – although the Arch Cru fund was not solely a private equity fund the point is that had it been invested correctly and responsibly, whilst it would have fallen in value, it would have recovered by now.
- Its adviser (who had lost considerable sums having personally invested in the fund) had left Willow (after some twenty years) and has had counselling for distress. The adviser had not been recognised for the great work he had done for Mr B in the past.
- Willow referred to other instances where although, in hindsight, investors would have been well advised to sell certain investments before suspension or collapse, there is no suggestion that advisers were at fault in recommending such investments. There was no difference between those cases and the collapse of the Arch Cru fund except that there was no '*deep pocketed*' company to make good investors' losses.

Willow also made further detailed submissions focussing on risk and responsibility, due diligence and the FSA Handbook. What follows is necessarily a summary of Willow's main point. Willow also raised a number of questions to which it seeks specific answers. In summary:

- Willow relied on information and fund fact sheets provided by regulated third parties and was entitled to do so. If it cannot use the risk categorisation offered by any third party or body as part of its consideration, then this surely throws into question both the risk descriptions of all funds and the accurate definition of risk itself.

- The advice was based on the scheme prospectus and management structure, the investment approach outlined in the fund manager reports, the flexible approach to be taken to asset allocation, the IMA cautious managed categorisation, confirmation from Capita that the fund was "cautious managed" with a corresponding asset allocation, actual performance based on published pricing and fund manager updates, absolute and risk adjusted performance assessments, and ongoing meetings with the fund manager, their representatives and the directors of Arch Investments.

- A basic principle contained in the FSA OEIC handbook is that one of the main reasons to use an OEIC is to achieve investment efficiency and diversification. Willow was entitled to rely on this basic premise. If not, the fund should never have been authorised.

- Increasingly the evidence suggests the losses of the fund have been caused directly and in the main by a combination of misleading and inaccurate fund factsheets and investment reports issued throughout the duration of the fund, mispricing of assets throughout the duration of the fund's operation and management and mismanagement of the fund beyond its investment mandate.

- The FSA requirements for signing off an OEIC say a fund must *"have been reasonably able to meet the objectives set out in its deeds and prospectus."* The ombudsman is indicating that this is not the case so there are surely a number of questions to be asked about the authorisation of the fund being fit for the purpose intended.

- There may have been a fundamental breach of process at the point of authorisation regarding fund benchmarks. Public listed benchmarks were deemed to be acceptable to use for private asset investments.

- With regards to the comment that the client and adviser may have some claim against the fund manager, misrepresentation of information from authorised parties is the responsibility of the authorised corporate director (ACD) according to FSA guidelines.

- If losses arise as a direct result of misleading material issued by authorised regulated third parties, mispricing, mismanagement of funds or fraud of the manager it is not the adviser's responsibility to cover these losses and then claim back from third parties.

- The notion that the ombudsman may reach its own conclusion as to what is "fair and reasonable" without being limited to the rules of common law is an interesting one and would be of great worry to any financial adviser.

- Although not legal experts, Willow's basic understanding is that it cannot be held responsible for losses that arise that are not "reasonably foreseeable" and are as a direct result of other third party negligence outside Willow's immediate control (the fact that an investor who put money directly into this fund would have suffered the same losses shows that the causation of loss is from the fund management). If this is not the case this has serious ramifications for the industry as a whole and would change the current accepted standards of practice in the industry and would surely have serious consequences for Professional Indemnity insurance and, taken a stage further, the long term viability of the independent advice sector in the UK.

- It asked why the IMA categorisation, fund factsheets, the ACD confirmation of the asset allocation of the fund, fund manager reports and fund pricing and performance cannot be taken into account when carrying out an assessment of risk.

- Would the ombudsman agree that the pricing of a fund is vital as it constitutes past performance, current performance and the decision to invest, with how much, and to remain invested, and with how much? The pricing of the fund and its performance supported its risk rating over more than two years. If the fund pricing was wrong would this not be a breach of FSA OEIC rules?

- Taking into account the provisions of the FSA OEIC handbook, is Willow not entitled to rely on the price of a fund being correct and to not be held responsible if the price is incorrect?

- The fund was an OEIC so by allowing one investment of over £150 million to be made into a Greek shipping company the fund manager and ACD nullified the most basic reason for using an OEIC, namely diversification to avoid excessive exposure to a single asset. (Willow has provided a copy of the particulars of claim lodged against Arch Financial Products LLP by cell companies in which the Arch Cru funds invested which refers to an investment of $167m in shipping related investments).

- Willow could not have reasonably foreseen that investments of the kind above would be made. Was the investment within the deeds and prospectus of the fund and did Arch's lawyers advise Arch not to proceed with the investment? Could Willow have predicted that legal advice would be ignored? Was this investment made in breach of OEIC rules, and if so who is responsible for any loss caused?

- Why did the ACD confirm that the fund was correctly categorised as cautious managed? If the ACD of any fund issues wrong information is the ACD responsible or the adviser?

- The risk management strategy, namely to place highly diverse and collateralised lending, was not followed.

- Canada Life carried out comprehensive due diligence before including it in their selected range of funds in their investment bond and came to the conclusion that the fund was low to medium risk.

- Does not the presentation of the January 2009 Investment Report by Arch at its meeting with Willow in London count as misrepresentation?

- If it was so obvious that the fund was "high risk", as the FSA asserts, why did it authorise the private finance fund for launch in November 2008? There is significant expert opinion to say the FSA's assertion is incorrect. Is it not interesting that so many top advisers with unblemished track records got their assessments of the fund so wrong at the same time?

- Is it fair to say that market risks did not change significantly after September 2008 although such changes brought down major banks in the UK and US, and has this not had an effect on the way the fund has behaved?

- In the light of the 119 page particulars of claim document it is '*staggering' to say "whilst much press and other comment has been made about the conduct of the Arch Cru fund managers, I am aware of no formal findings on these points that I should take into account in assessing compensation here."* The apparent investments into Greek shipping companies seem bizarre and are reported to be via a Greek shipping entrepreneur who had a terrible history of failed projects and large investor losses.

- Unless it can be concluded definitively that the fund was *not* negligently or fraudulently managed, no judgment can be made on the case.

- Given the legal action the cells are taking to recover the losses, how can the losses be the responsibility of the adviser? Why is there no reference to this in the adjudicator's letter?

- If the observations about the general appropriateness of the fund for retail investors are true, why was it authorised and why did the FSA not pick up on such obvious flaws?

- The FSA handbook said that the ACD shall ensure that taking account of the investment objectives and policy of the company as stated in its most recent published prospectus, the scheme property of the company provides a prudent spread of risk.

- Capita knowingly became the majority or sole shareholder in the cells so by definition there would be no liquidity in the shares of those cells, yet it declared to would be investors that there was "…*little liquidity risk*". As ACD it had a responsibility to know what was going on in the cells given the liquidity repercussions to investors.

- Capita's annual short report of June 2008 states: *"There are no borrowings or unlisted securities of a material nature and so there is little exposure to liquidity risk".* It also says the ACD *"reviews policies for managing these risks in order to follow and achieve the investment objective"* namely *"to generate consistent returns to provide wealth preservation and capital appreciation."*

- Capita's statement that *"there are no unlisted securities and little liquidity risk"* is not consistent with recent statements that it did not know what the Guernsey listed cells were investing in.

- How can the ombudsman accept Capita's statement that *"the IMA has made clear that its sector categories do not imply anything about the level of risk associated with a particular fund"* when there are suggestions that the ombudsman has also upheld other complaints purely on the basis that a client's preferred risk rating was not in line with the IMA category.

- Willow referred to the FSA handbook and to various rules and provisions it says apply to the running of an OEIC. These relate to the role of an ACD, a prudent spread of risk being provided by funds, investments being in accordance with the prospectus, the accuracy of prospectuses, liquidity requirements and record keeping.

- A vital part of any decision to invest and stay invested will be the fund reports and monthly performance. There have and continue to be clear questions about not only pricing leading up to suspension but also pricing throughout the history of the fund, evidenced by allegations in January 2013 against the fund auditors.

- The actual published audited performance of the fund was, over a period of nearly three years, similar to that to be expected from a cautiously managed fund. Right up until suspension the fund had consistently displayed superb risk adjusted performance.

- During the *credit crunch* additional due diligence was undertaken – detailed questions were asked about the valuation basis for the fund, the spread of risk and the impact of the credit crunch on fund stability and liquidity. The answers received, combined with fund managed reports, Capita's shortened investment report in December 2008, the Guernsey Cell accounts and directors statement, Willow's meeting with the Arch directors and the detailed fund investment report in February 2009 led Willow to believe that it was safe to continue to remain invested in the Arch Cru fund.

- The only rationale for advisers being held responsible was on the basis that the fund was recommended as a low risk fund, not a high risk fund. In order to conclude that the fund was high risk the adviser would have had to disregard published information (by the IMA, FSA and Capita) and conclude that the investment and diversification strategies detailed in the fund prospectus would not be followed at all. Willow queried why so many advisers apparently '*got it wrong*' by failing to see that it was a high risk fund (and when Capita and other parties were apparently unaware of the issues affecting the underlying funds until after suspension).

- The fund fact sheet for October 2007 said "the objective of our flagship fund is to generate consistent returns, that particularly when viewed over the medium to long term (minimum 5 years plus) exceed cash returns by 4% per annum net of fees." Although the fund fact sheets indicated that it was hoped to achieve higher potential returns Willow did not advise on that basis and indeed warned clients to focus on base target of 4% per annum above cash deposits.

- Even if the fund was high risk, this would not remove the obligation of the fund manager to comply with the principles of an OIEC or the ACD to carry out its role in overseeing and protecting assets – fundamental requirements which were breached and which could not have reasonably been foreseen by a competent adviser. The investment of a large

proportion of the fund into Greek Shipping (and no doubt other less obvious irregularities) caused the majority of the losses, a detailed breakdown of which was requested.

- The FSA had power to revoke a fund – the Arch Cru Private Finance fund was authorised in October 2008, only six months prior to suspension. If the FSA had reviewed that fund in conjunction with other operations at Arch and if the risks should have been so obvious to advisers why did the FSA say nothing at that point?

- The adviser relied on information that he was entitled to rely on, provided by regulated parties, that was clearly wrong – the fund was mismanaged and exposed to specific risk and liquidity risk with high exposure to unlisted securities.

my findings

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

I have included above only a brief summary of the complaint background, but I have read and considered all the evidence and arguments available to me from the outset, including those submissions made since I issued my provisional decision, in order to decide what is fair and reasonable in all the circumstances of this complaint.

I note that Willow has asked for specific answers to some of the points it has raised, some of which are very general in nature. My role is to determine this complaint on the basis of what is fair and reasonable in the particular circumstances of Mr B's case. So although I have carefully considered all the points Willow has made, I confine my comments below on what Willow has said to what I consider necessary for the fair determination of this complaint.

I must decide this complaint on its individual merits. But this service has considered complaints about Arch Cru funds before and published a decision which sets out our general approach to such complaints on our website. The decision is in the investment section of our online technical resource which can be found by clicking the publications tab.

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.

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

As Willow gave advice about a regulated investment, 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.

There is no dispute that the investment decision Mr B made that is the subject of this complaint, was made on the advice given to him by Willow and that Willow assessed the suitability of the products and investment fund for Mr B.

So, taking the relevant considerations into account, it seems to me that the overarching question I need to consider in this case is whether the recommendation given was a suitable recommendation for Mr B in his particular circumstances.

In deciding this question I need to take into account the nature and complexity of the investments and Mr B's financial circumstances, needs and objectives; understanding and relevant investment experience; and tolerance to investment risk.

If having considered all the relevant circumstances, I find that the recommendation, or any part of it, was unsuitable for Mr B. I then need to consider:

- whether he relied on the recommendation and has lost out as a consequence of that (by considering what he would have done 'but for' the poor advice) and
- if he did, how fair compensation should be calculated in all the circumstances of the case

Having considered the matter very carefully and particularly in the light of Willow's further comments, I have concluded that Mr B's complaint should be upheld for substantially the same reasons as given in my earlier provisional decision.

I set out below my rationale, taking into account all of the available evidence. Some of what I say echoes earlier comments. As I have said, and although I appreciate that Willow may find my approach unsatisfactory, I have not commented on each and every point raised by Willow. But, in broad terms, Willow's objections centre upon its legitimate reliance upon information provided by other parties and its contentions that Mr B's losses were caused by the actions, inactions or negligence of other parties and that such losses were not reasonably foreseeable. All of those matters are considered below.

Information such as fund factsheets was freely available to professional independent financial advisers with information about how, generally, the Arch Cru funds would operate and the nature of their investments.

The fund initially recommended was the Arch Cru Portfolio. The broad constituents of the fund at the time the advice was given were:

Private Equity	33.6%
Private Finance	33.3%
Sustainable Opportunities	13.1%
Real Estate	14.8%
Cash (committed)	5.4%

I maintain the view set out in my provisional decision that private equity investments carry a fairly significant risk of capital loss as well as gain.

Willow seems to concede that private equity investment on its own is likely to be a high risk investment. I share the understanding that such private equity investments carry a significant risk of capital loss as well as gain. I also agree that any non-UK equity holdings would also carry exchange rate risk. Moreover, that the equity stakes are not quoted on public markets would seem to make them inherently less liquid, bringing an additional element of risk.

Willow says the fund managers' approach, properly understood, meant that the performance of the fund would be much more controlled than might otherwise have been the case with private equity investments, as it says it was during 2008. But in my view the performance of

assets over one short period of time should not be taken as reasonable evidence to suggest that a fund with exposure to these could be reasonably sold to a consumer like Mr B on a low to medium risk basis. While perhaps not unusual for private equity investments, the nature of the risks was opaque and hence more difficult to judge as the precise nature of the holdings does not seem to have been disclosed.

As I noted in my provisional decision, firms who, for whatever reason, did not wish to raise money from more conventional sources such as banks or sales of shares, took out loans that the private finance element of the fund invested in. It is apparent that if in making such investments the fund manager provided lending to companies that entered difficulty or failed, then significant reduction in capital could occur. Indeed an asset aiming to produce *"double digit returns"* would also be expected to involve significant risk.

The sustainable opportunities element of the fund appears to have been themed investment, equity and otherwise, in *"environmental, social and economic trends."* Equity investments and investments limited and concentrated by theme would appear to have the potential to lead to significant losses.

So having carefully considered the available evidence I find on balance that the large proportion of the investment in private equity and private finance meant the recommended investment involved significant and unusual risks to capital, which to my mind imply higher risks than Mr B was willing to accept.

I am satisfied that Willow, being a professional independent financial adviser, ought reasonably to have identified these facts, features and risks from the material readily available at the time, and taken them into consideration when giving its advice.

As I noted earlier, the potential problems with these types of investments were laid bare by the market conditions of the last few years and are now well known. So it is important to avoid the benefit of hindsight in the assessment of these matters today. However, this was an unusual type of fund, operating in a very specific way and with a limited track record. It could suffer significant losses, the nature of which would be difficult to predict or estimate at outset.

I do not overlook the statement by Capita referred to by Willow to the effect that there would be *little liquidity risk* and the point that Capita's majority shareholding in the cells would by definition mean there would be no liquidity in the shares of those cells. But it seems to me that, given the nature of the investments the fund was contemplating, it would have been foreseeable that liquidity issues could arise in any event.

I have considered Willow's suggestion that to be '*signed-off*' by the then FSA a fund must *"have been reasonably able to meet the objectives set out in its deeds and prospectus"* and Willow's point that it expected the fund's stated strategy to mitigate the risks that might otherwise affect the fund. But notwithstanding any generalised assurances of conservatism, and consistent positive returns by the fund managers, the Arch Cru investments contained a large proportion of what might reasonably be described as sophisticated and/or complex investments the nature of which was opaque. The fund as described was not suitable for an investor uncomfortable with its particular, unusual risks.

Regardless of how the fund was generally categorised by the IMA or by companies who included the fund as an option within their product offerings, Willow had a responsibility to ensure that the recommendation it made was suitable for Mr B. The IMA's classification of

the fund did not mean the fund could not suffer significant losses as a result of risks that were apparent as I have described above. That classification was not in itself sufficient grounds for concluding that the fund was suitable for Mr B.

So, having very carefully considered the points raised by Willow, I remain satisfied that, being a professional independent financial adviser, it ought reasonably to have identified, from the readily available description of the fund, risks of the kind I have described and concluded that they made the fund unsuitable for Mr B.

I am satisfied that Willow, being a professional independent financial adviser, ought reasonably to have identified these risks from the readily available description of the fund that was available at the time and taken them into consideration when recommending the investment. Although Willow did identify that the fund was complex in structure and relied heavily on private market investments, it appears that Willow did not then go on to consider whether that meant that the risks were such that the fund's risk profile was not as described.

Mr B was a low-medium risk investor. Indeed, his personal client questionnaire stated he had a low risk to pension planning. It was his objective to take as much income as possible from his pension fund and he was fully aware that it was gradually eroding as a result. But tolerance of such gradual losses did not in my view amount to a willingness to risk significant fund depletion through exposure to higher risk funds.

The recommendation report did illustrate that the underlying structure of the Arch Cru funds was complex. It also mentioned its '*heavy reliance on private market investment*s'. But I am not persuaded that this, or the other information provided, was such that Mr B appreciated the relevant risks. Knowledge that the fund included private market investment does not equate to an understanding of the risks that might entail.

Overall, I do not believe it likely that Mr B appreciated the nature of the risks and I am not persuaded that the investment was suitable for him – I think it is unlikely that he would have been prepared to accept the kind of losses this product could generate.

I am satisfied that this recommendation exposed Mr B to significant risk, exposed to asset holdings that were, in my opinion, non-standard and potentially specialist. I have concluded that this was risk of a kind that the evidence suggests Mr B was not willing to take. In my view Willow should have identified this and so should have realised that the recommendation was unlikely to be suitable for an investor like Mr B. I say this not withstanding the fact that the sum involved does appear to have been a small proportion of Mr B's overall wealth.

I have not seen anything which suggests to me that Mr B would have invested in the Arch Cru fund if it had not been recommended to him.

Having carefully reviewed the evidence in this case, I cannot now identify the precise investment decision or decisions Mr B would have made upon appropriate advice. But having considered his circumstances, objectives and attitude to risk at the relevant time, on balance I am satisfied that he would have sought a return on his invested money within his previous arrangement (from which he transferred in order to access the Arch Cru fund). Having considered his circumstances and objectives at the time, I think that Mr B would have invested his money in a fund similar to his previous provider's 50/50 Cautious Managed fund.

On that basis I am satisfied it would be fair and reasonable for Willow to make good the loss Mr B has suffered because his money was invested inappropriately.

In reaching this conclusion I am mindful of Willow's suggestions that Capita misrepresented aspects of and failed to properly oversee the Arch Cru funds and so caused and is to blame for Willow's advice and the current position of the Arch Cru funds. I have also taken account of its suggestion that the FSA as it then was should have acted differently or earlier to minimise losses (for example Willow says it should not have closed the fund). Willow has made it abundantly clear that it considers that others were responsible for Mr B's losses and that it is unfair to expect Willow to shoulder the majority of the loss.

I have also considered whether the losses on the Arch Cru fund were foreseeable because of the extreme market conditions that existed at the time. Given the make up and investment strategy of the Arch Cru fund as described in this case, I share the view that this fund could have suffered significant losses in a wider range of market circumstances than the (relatively) extreme conditions that we have observed since 2008. The risks were all risks that an experienced IFA should have noted and taken into account in their deliberations.

As to the actions of the fund managers I am aware that a range of comments and allegations have been made. These are not questions that I am in a position to determine in this dispute – and indeed I have no jurisdiction to consider a dispute between an IFA and a product provider or fund manager. However these considerations may in principle be relevant to the determination of fair compensation. So I will reiterate some general observations with which largely Willow will already be familiar (and which are not, and are not intended to be taken as, any comment on the conduct of the managers of the Arch Cru funds).

It is inherent in a managed fund that there can be criticisms of the judgement and skill of the fund managers – indeed the ability of the fund manager is one of the risks that is inherent in a managed fund. That some will manage the fund poorly (or even very poorly) is in my view an inherent and foreseeable risk. In extreme circumstances the way a fund manager performs may fall outside the normal range of professional performance. Indeed Willow says that the boards of the cells and the ACD mismanaged and mispriced the cells.

Two broad circumstances might arise. First there may be material mis-representations upon which an adviser has relied in giving advice to his client. In such circumstances it seems to me that both the client and the adviser might have some claim against the fund manager or the party for whom the fund manager is acting such as an ACD (but a dispute between the adviser and those parties could not be considered by this service).

Second, there may in principle have been negligence or fraud in the conduct of a fund. Such actions might represent a break in the "chain of causation" – that is the losses arising from the negligent initial advice may not fairly be taken to include all of the losses that the customer has suffered, because of the separate negligent or fraudulent acts in respect of the management of the fund.

My approach to such cases 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 (even if the fund is subsequently poorly or even fraudulently managed). But, secondly, and in contrast, particular difficulties arise in assessing fair compensation when it seems clear that 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 negligent adviser as putting the customer back in the financial position they would have been in but for the poor advice notwithstanding the arguments around possible breaks in a chain of causation. Again in principle there may be causes of action of either the adviser or the client against the fund manager (or the fund manager's principal) in such circumstances (but again I cannot consider a dispute between an adviser and such a party).

In the present case there has been much press and other comment made about the conduct of the Arch Cru fund managers. I have also taken account of censures the FSA has issued such as to Capita for its failings in relation to the Arch Cru funds between June 2006 and March 2009.

However, taking account of my general approach outlined above, I consider that Mr B would not have been in this particular investment had it not been for the unsuitable advice given by Willow. Advice that in my view was unsuitable for him. It follows that notwithstanding any failings on the part of the fund managers, I consider it fair and reasonable that Willow should be responsible for putting Mr B back in the financial position he would have been in but for that poor advice.

I have considered Willow's points about the actions or inaction of the FSA but having done so I see nothing there that would justify me limiting the compensation payable to Mr B in this case.

I am mindful, though, that Capita, HSBC Bank and BNY Mellon Trust & Depositary have established a payment scheme for Arch Cru fund investors, administered by Capita. Investors have until 31 December 2013 ordinarily to apply for payment under the terms of that scheme, which was agreed with FSA. I am satisfied it would be fairest to take into account the entitlement Mr B has under this scheme when deciding what is fair compensation in the circumstances of his case – he would not have been entitled to that money if he had not invested in the Arch Cru fund.

I have considered Willow's objections, but I still share the view that if Willow considers other firms caused or contributed to the overall loss it will incur, then it can pursue those firms. I do not believe Willow would be materially disadvantaged in that regard if Mr B chose to accept the compensation to which he is entitled under the Capita administered redress scheme.

In awarding redress I have assumed that, with reasonable advice, Mr B would have invested the original capital in a fund like his previous provider's 50/50 Cautious Managed fund instead of the Arch Cru fund and that the rate of return on the capital would have been equivalent to the return on the 50/50 Cautious Managed fund from time to time over the period.

Neither Willow nor Mr B's representative has raised any material objection to the use of this rate (although I do not overlook that during the course of our investigation the use of Bank of England base rate plus 1% was also suggested by the adjudicator as a possible alternative).

The Arch Cru fund is currently illiquid and so Mr B is unable to mitigate his losses by realising the investment. In the circumstances I would normally direct that, as part of the redress, Willow should purchase Mr B's investment in the Arch Cru fund. But because Mr B's current provider is unable to facilitate this and is unable to accept a compensation payment I have made alternative directions.

my final decision

For the reasons set out above, my final decision is that I uphold Mr B's complaint. And, in full and final settlement of the complaint, I direct Willow Financial Management LLP to pay him compensation as follows:

1) Willow should work out the value that the money invested in the pension in Arch Cru fund would have had if it had instead performed in the same way as Mr B's previous provider's 50/50 Cautious Managed fund between the time it was invested and the date of settlement, allowing also for any amounts paid out from those funds from time to time by way of withdrawals, distributions of capital or before-tax income. I will refer to this below as (A).

2) Willow should obtain from Capita an estimate of the current encashment value of the Arch Cru fund (albeit that it cannot in fact be encashed). I will refer to this below as (B).

3) Willow should work out the financial loss to the pension by subtracting (B) from (A). It may also deduct from this the compensation Mr B is entitled to and could obtain via the redress scheme for investors in the Arch Cru fund, operated by Capita in respect of Capita, HSBC and BNY Mellon (which I will refer to as (D)). I will refer to the result ((A) minus (B) minus (D)) as (C). If Mr B has already received payment under that redress scheme then this should be taken into account as at the date it was actually received. If the redress scheme is withdrawn before 31 December 2013 preventing Mr B from limiting his losses, then if he has not already received payment under the scheme, Willow should within 56 days pay (D) direct to Mr B as a cash sum.

4) Ordinarily I would direct Willow to pay a sum into Mr B's policy so that its value increases by (C). But Mr B's current provider has said that it is unable to accept the compensation payment. So instead Willow should make a cash payment to Mr B equivalent to (C) less a deduction representing tax at Mr B's highest marginal rate. That deduction is to allow for the fact that had the money been paid into his policy and then paid out as income it would have been taxable. So if Mr B is a basic rate taxpayer then a deduction of 20% may be made.

5) As set out above, I would normally say that Willow should purchase the Arch Cru investment so that ownership of the Arch Cru holding is transferred from it to Mr B by Willow paying an amount equivalent to Capita's valuation (B) into Mr B's current policy. Capita has informed us that it has no problem with the ownership of the Arch Cru holdings being transferred to another party. But Mr B's current provider has said that it is unable to facilitate this. Therefore, in addition to (C) Willow should also pay to Mr B the current encashment value (B) of the investment in the Arch Cru fund holdings. Again Willow may make a deduction in respect of income tax at Mr B's marginal rate.

6) In exchange, Willow can require Mr B to provide an irrevocable undertaking to pay it such sums as are realised or become realisable in respect of those investments as and when they are realised or become realisable. I would ask Mr B to note that carefully. My understanding is that any further distributions will be paid into his current arrangement and so he should be aware that he may need to realise other assets in order to meet the terms of any undertaking given to Willow.

7) Interest at 8% simple pa should be added to any sums unpaid after 42 days after my final decision.

If Mr B accepts this decision, he will need to cooperate with Willow to provide evidence

about payments from the fund and from the Capita redress scheme to ensure that the redress I have awarded can be paid promptly.

Lesley Stead
ombudsman