Complaints Commissioner

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14th April 2015

Dear Complainant,

Complaint against the Financial Conduct Authority
Reference Number: FCA00038

Thank you for your emails of 28th November 2014 and 15th March 2015.

As the rules of the scheme under which I consider complaints can be found on our website at www.fscc.gov.uk, I do not intend to set them out fully below.

Your complaint

From your email and the papers you have submitted to me and the FCA I understand that your concerns relate to the fact that:

- You believe that the regulators, the Financial Services Authority (FSA) and the Financial Conduct Authority (FCA), failed to supervise your independent financial adviser Firm PM adequately, and allowed Firm PM to trade without Professional Indemnity Insurance (PII) cover for around 18 months before the firm's authorisation was withdrawn.

- You are also unhappy with the conduct of Firm PM's PII provider as they have cancelled the firm's cover and are now refusing to pay any claims.

My position

Before I comment on the specific issues you have raised, it may be helpful if I make some general comments about the regulatory system.

The regulator operates a risk based approach to regulation. Given the number of firms which operate within the UK's financial services industry it is not possible for each firm to have a dedicated supervisor who is responsible for monitoring that firm closely.

Under the regulator's approach, only the firms which are deemed to pose the largest regulatory risk will have a dedicated FCA supervisor. This means that by their size, nature and potential impact they may have, generally only the major banks, large asset managers and the major insurance firms are firms which have a dedicated supervisor. Additionally, a small firm which is deemed to pose a high risk to consumers and which is under close scrutiny by the FCA (usually a firm about which the FCA has significant concerns, or firms where there is continuing regulatory action) may also be given a dedicated supervisor.

As it is not possible for the FCA to monitor closely every firm it regulates, the FCA has adopted a system where in addition to conducting periodic 'inspection' visits it asks firms to regularly provide it with significant amounts of information which enable it to monitor the conduct of the firm. Key operational information is collected at six-monthly intervals with further information, which is used to set an individual firm's regulatory fees, being collected on an annual basis.

The regulator reviews the information which firms provide and, if it has concerns arising from this, may ask the firm to provide further information, change the firm's reporting regime (by asking for information on a more regular basis), or conduct further ad hoc visits to the firm to allow further investigation into its concerns. The FCA will also consider any additional information it receives from other sources such as consumers, compliance consultants and the Financial Ombudsman Services (FOS).

I know that you feel that the FCA's supervision of Firm PM was inadequate as it was only conducting four yearly touch points or inspection visits. Whilst the FCA did undertake a visit to Firm FM in 2010 which identified some weakness in Firm PM's procedures, specifically in relation to the FCA's Treating Customers Fairly initiative, the FCA felt that these weakness could be addressed without the need for formal (disciplinary) action. Whilst the inspection visit was completed in 2010, the FCA had been monitoring the firm's conduct by way of its statutory powers, through Firm PM's external compliance consultant following the TCF visit, and through the use of detailed six monthly reports which the firm was required to submit. The FSA was not simply relying upon a telephone call every four years to monitor Firm PM, as you suggest.

I appreciate that you also have concerns about the manner in which Firm PM engaged with its compliance consultancy service between 2005 and 2010. In general terms, how a firm engages with its contracted compliance consultant is a matter between it and the compliance consultant; and it was not until the TCF visit in 2010 that the FCA became aware of some issues.

You have commented that the regulator allowed Firm PM to trade without any PII cover. Whilst it is the case that the firm did trade without PII, this was done without the regulator's knowledge. As I have indicated above, due to the number of firms the regulator supervises it undertakes a risk based approach to regulation and uses six monthly reporting as a way of supervising the firms which are deemed to pose a lower risk. Firm PM fell into this category.

The last return Firm PM submitted before the issues arose was for the period ending 30th June 2012. The information contained within that report showed that the firm held the appropriate PII cover. I would add that that information would appear to have been accurate and correctly reflected Firm PM's circumstances, as I understand that Firm PM's PII policy expired on 21st July 2012 which was after the end of the reporting period. At that time, there was nothing to suggest that Firm PM was trading without PII cover.

It was not until the report for the period ending 31st December 2012 became overdue that the FCA would or indeed could have had any cause for concern about that matter. As the reports the regulator requires firms to submit include a considerable amount of information, some of which will not be available for several weeks after the end of the reporting period, the regulator allows firms several weeks to submit their returns. In this case, Firm PM was required to submit its return for the period ending 31st December 2012 to the FCA by 12th February 2013. Unfortunately, Firm PM failed to do this.

The regulator's usual practice is that once a return becomes overdue, a note is automatically added to the FCA monitoring system and an overdue notice is issued to the firm. In many cases the receipt of the overdue notice (which is usually issued about a week after the return becomes overdue) prompts the firm either to submit the required return or, as happened in this case, to contact the FCA.

In this case, although Firm PM's 31st December 2012 report was late (and had been identified as a late submission), Partner P contacted the FCA on 20th February 2013 and indicated that he wished to stop conducting regulated activity (which effectively means ceasing to offer advice to its clients), and asked how to go about cancelling Firm PM's authorisation. This, together with the overdue return, raised concerns with the FCA and as a result the FCA started to make further inquiries of the firm.

The FCA has provided me with full details of the interactions it had with Firm PM and a number of Firm PM's customers between February 2013 and February 2014. I appreciate that it would assist your understanding of the situation if I were to provide you with further details of how the regulator engaged with Firm PM between February 2013 and January 2014 but this is not something I am able to do in detail. This is not because I wish to be unhelpful but because of the constraints of Section 348 of the Financial Services and Markets Act 2000[1]. However, as Firm PM is no longer authorised by the FCA and has ceased trading I can add the following information.

Whilst Firm PM remained authorised by the FCA (until 27th February 2014) I understand that it had entered into an agreement to vary its permissions and was not undertaking any regulated activity. Unfortunately, although it appears that the FCA entered into an agreement with Firm PM to vary its permissions, I have been unable to locate written confirmation of if and when this formally took place. This is clearly a weakness in the FCA's handling of the case, although the failure of the FCA to clarify if and when this agreement was reached does not affect my assessment of your complaint, since such an agreement would simply prevent the firm from conducting further regulated activity (i.e. providing advice to consumers), which I understand that it was in any case not undertaking. Such an agreement would not have prevented the firm from complying with its outstanding liabilities.

I would also add that by entering into an agreement with Firm PM to vary its permissions, the FCA took the view, correctly in my opinion, that it would be inappropriate to immediately cancel Firm PM's authorisation as it was aware that there were a number of outstanding Financial Ombudsman Service (FOS) complaints (including the claims monies which were due to you). Cancelling Firm PM's authorisation when there were outstanding FOS complaints would reduce the action which the FCA could take to ensure they were handled appropriately.

Although I believe that the FCA took the correct action in this regard, it is unfortunate that circumstances (the bankruptcy of Firm PM's partners) prevented the FCA from using its powers to ensure that the FOS awards were complied with. Once Firm PM's partners had been declared bankrupt (and their assets transferred to trustee in bankruptcy) there was nothing further the FCA could do and as a result it cancelled Firm PM's permissions.

[1] Rehearsed within SS 16 to 19 of Part 2 of the Financial Services Act 2012

I would also add for the sake of completeness that although delays in settling awards made by the FOS are a cause for regulatory concern, particularly where the award is large and is to be settled by the adviser's PII provider, regrettably a delay is not entirely uncommon. Clearly where the sums are large, as I understand was the case in relation to the awards which the FOS made to you, a firm is often unable to provide the redress from its own resources and must seek settlement from the PII provider first. As the firm has to liaise with the PII provider and the PII provider has to accept, authorise and issue the settlement, this can take several weeks (and in some cases longer).

Nonetheless, continued delays are rightly a cause for concern and when the delays in settlement of Firm PM's FOS awards were raised with the regulator, I understand that it did engage with Firm PM in an effort to arrange settlement. It is unfortunate that, despite the FCA's best endeavours, Firm PM failed to settle your complaints and make the awards the FOS had instructed it to do. However, it must be remembered that, had the FCA cancelled immediately Firm PM's permissions (authorisation), it would not have been able to engage with Firm PM in an effort to secure the payment of the FOS awards.

I accept that you entered into correspondence with the FCA in June 2013 in an attempt to seek enforcement of the awards the FOS had made. Whilst it is extremely regrettable that payment was not made, given the size of the awards recommended by the FOS, any delay in settlement could, to a degree, be explained by the fact that Firm PM had referred the matter to its PII providers. I would also add that the bankruptcy of Firm PM's partners suggests that, even if the FCA had wanted to take further action to ensure the payment of the outstanding FOS awards (if settlement could not be obtained from its PII provider), this would not have been possible.

I am also aware that you are unhappy that Firm PM's PII provider has declined its PII cover, which has had severe impact upon your financial position as you are no longer able to enforce the award which the FOS made to you. This is extremely unfortunate but this is not the fault of the FCA.

Firm PM's PII provider, like any insurance company, will underwrite (or assess the potential risk) before deciding to offer cover and set a premium. In doing this the insurance firm asks the firm to provide certain information (in much the same way as a motor insurance provider would do) and will assess the risk based upon this information. Where the insured (in this case Firm PM) provides incorrect information or fails to disclose material facts which would have affected the provider's decision to offer cover at the underwriting/assessment stage, the PII provider (like a motor insurer) has the right to decline cover.

From the information I have been given it appears that when taking cover Firm PM (rather than the regulator) failed to inform its PII providers of material information which would have affected the insurer's decision on whether it wished to offer cover. I understand that the PII provider has therefore made the decision that cover should be withdrawn. For the sake of completeness I would add that the provision of incorrect advice would not, on its own, void a PII policy as the PII policy is amongst other things designed to provide financial cover in the case of an adverse FOS finding.

Although PII cover benefits consumers, the legal position is that PII cover offers protection to the business against claims arising out of errors or incorrect advice. Whilst usually the withdrawal of PII cover would not result in a problem, as responsibility for claims would simply pass to the business, in this case the fact that the business has failed (and the partners declared bankrupt) has resulted in the problems you are now facing.

Although I have considerable sympathy for your position, the FCA cannot instruct Firm PM's PII providers that they must honour your claim. If you feel that the PII provider has acted inappropriately in making the decision which it has made then I can only suggest that you obtain legal advice (which will be at your own cost) about how you may be able to challenge the PII provider's decision and enforce any rights you may have under the Contracts (Rights of Third Parties) Act 1999.

In your email of 15th March 2015 you have commented that you believe that it is "contradictory and misleading for the FCA to make the following claims:-

> *We regulate the financial services industry to ensure firms stick to the rules and consumers don't fall victim to scams or get tied in to unfair contracts*
>
> *[…]*
>
> *We work closely with firms to fight financial crime*
>
> *[…]*
>
> *Understand that we will take action against them if they use corrupt or unethical methods*
>
> *[…]*
>
> *We regulate most firms and individuals that advise on, sell and arrange financial products and services. If a financial firm or individual fails to meet the standards or follow the rules we set, we can take action against them.*
>
> I claim that no action was taken other than a 'treating customers fairly' assessment in 2010, which you infer was not sufficiently important as to warrant disciplinary action".

Whilst it is extremely unfortunate that you have suffered a considerable financial loss, this appears to have resulted from what the FOS has ruled was poor or incorrect financial advice provided by a regulated individual rather than as the result of financial crime, fraud, or a scam. In my view, the loss you have incurred was not the fault of the regulator: it is inevitable that in any risk-based regulatory system, some poor practice or misconduct will occur. I have seen nothing to suggest that the FCA's decisions, on the basis of the information they had at the time, were unreasonable.. Although I accept that concerns were raised in 2010 following the completion of a 'Treating Customers Fairly' visit, the FSA made a decision that the concerns raised did not require formal disciplinary action but could be addressed by working with Firm PM's compliance consultant. The papers presented to me show that Firm PM did engage with its compliance consultant at that stage, and that the compliance consultant's involvement addressed the FSA's concerns.

Conclusion

Having considered your complaint, although I have a great deal of sympathy for the position you now find yourself in, I have concluded there is nothing to indicate that the FCA has acted inappropriately or failed in its statutory duty when supervising Firm PM.

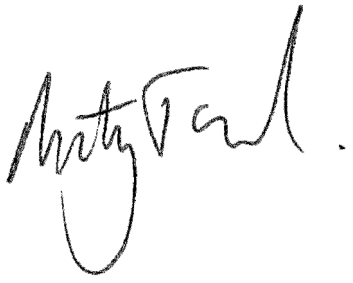
I have drawn attention to the FCA's failure to identify written confirmation of Firm PM's variation of permissions, and I recommend that the FCA considers what steps should be taken to minimise the risk of a recurrence, but that is not a matter which affects your complaint.

There is one additional matter which, though not directly referred to my office, is something which I feel requires comment by me. When you complained to the FCA you raised concerns over the time it took the FCA to provide information which was originally requested under a Freedom of Information Act (FOIA) but which was then redirected to the Supervision Division.

The regulator has partially upheld that element and has accepted that there was a delay of one month (from early March and mid-April 2014) where there was neither significant activity nor any reason for a delay. However, having viewed the FCA's papers, I consider that there was a further delay of around two months (between May and July 2014). This delay in responding to the trustee in bankruptcy (who was requesting information on behalf of Firm PM's PII provider's lawyers) is disappointing. However, whilst I feel that it is important that this factual correction is made, and that the FCA considers whether this reflects a weakness in its procedures, I do not believe that it has affected the situation in which you now find yourself. I hold this view as at the time of the delays Firm PM, together with Partner P and Partner L, had already been declared bankrupt with all of their remaining assets already transferred to the trustee in bankruptcy

I appreciate that you will be disappointed with my decision but hope that you will understand why I have reached it.

Yours sincerely



Antony Townsend
Complaints Commissioner