Complaints Commissioner

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10 July 2017

Our Ref: FCA00127

Dear Complainant,

Re: Your complaint about the Financial Conduct Authority (FCA)

Thank you for your correspondence about your complaint against the Financial Conduct Authority (FCA). Please accept my apologies for the length of time it has taken to reach a decision in your case. A significant amount of work was undertaken both by my office and the FCA, at my request, in order to resolve this complaint, involving a review of a large quantity of documents. I issued a preliminary decision to you on 30th May, on which I invited your, and the FCA's, comments. In the light of the response which Mr A sent on your behalf, we have undertaken some further inquiries. I am now able to write to you with my final decision.

How the complaints scheme works

Under the complaints scheme, I can review the decisions of the FCA's Complaints Team. If I disagree with their decisions, I can recommend that the FCA should apologise to you, take other action to put things right, or make a payment.

As you can find full details of how I deal with complaints at www.frccommissioner.org.uk. I have not set them out here. If you need further information, or information in a special format, please contact my office at complaints@frccommissioner.org.uk, or telephone 020 7562 5530, and we will do our best to help.

Your complaint

In your complaint of 3rd March 2015 to the FCA and then to me of 4th May 2016, you said that the FSA had failed to supervise P and SM, later HG adequately (element one). Of special concern was that these firms appeared not to have had PII cover in place at the relevant times (that is, while they were still authorised by the FSA – element two). This resulted in customers of the firm, including you, not being able to claim on the PII policy which should have been in place to prevent consumers losing significant proportions of their investments over the Financial Services Compensation Scheme (FSCS) limit of £50,000.

The background to your complaint

You had been a long-standing customer of SM and did not have concerns about the way your and your wife's pension funds were operated for many years. Following the sale of SM to P, your pension funds were moved from an advisory service to "discretionary management", with your risk appetites assessed as moderate. Despite this, SM started investing much larger percentages of your pensions in high risk funds, which later turned out to be Unregulated Collective Investment Schemes (UCISs). In 2011 you became aware of this and concerned

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about the state of affairs. You requested that your investments were brought in line with your clearly stated risk tolerance. As matters did not progress to your satisfaction, both you and your wife made a formal complaint to SM in late 2011, which was rejected by the firm but upheld by an Ombudsman of the Financial Ombudsman Service (FOS) in June 2013.

The firm, now known as HG, went into liquidation a few days later and your losses as a result of non-payment of the FOS award stand at over £200,000. You referred your wife's complaint to the FSCS for compensation as her losses are below their compensation limit of £50,000 but your losses are much greater than this limit.

Your current financial adviser, Mr A, has been assisting you in managing your complaint against the FSA/FCA (from now on referred to as the regulator) in relation to SM/HG and the group of companies the firm belonged to and the regulator's apparent lack of action. The information in his supporting statement regarding the work he had done to warn the regulator of concerns about SM and the group companies from late 2011 was backed up with a printout of emails between him and the regulator (titles and dates only, not their content). You were, however, advised by the Complaint Investigator dealing with your complaint that his statement and the evidence provided were not relevant to your complaint.

The regulator did not uphold any element of your complaint. Having explained to you that most of the information which they had reviewed was confidential, the key part of the regulator's response was as follows:

> *I am able to assure you that the issues have been considered appropriately and I am satisfied that the Authority did not act unreasonably regarding this matter.*
>
> *Despite the fact that I am unable to comment on anything that happened after 2012 which relates to the P, I can confirm to you that P did have a suitable PI cover in place up until 2012. Having spoken to my colleagues in the Supervision team who had been closely working on the matters that you raised; and having reviewed the relevant records available, I am satisfied that the company completed all of the necessary regulatory returns up until 2012.*

You were dissatisfied with this response, and referred the matter to my office.

My findings

When I reviewed your complaint, I found the regulator's response to be inadequate. In my view, rather than attempting to get to the heart of your complaint, the investigators dealing with it focused their response on the PII status of the wrong firm. The structure and interrelationships of the various firms were complex, and it is true that you had identified the wrong firm as being key in relation to PII. However, this was not surprising, since you only had access to limited information. Members of the regulator's Complaints Team have access to all information relating to regulated firms and they should have demonstrated greater curiosity when assessing your complaint, and taken a holistic approach to ensure they understood your complaint fully and resolved all the relevant complaint points.

Having identified the above concerns, I offered the FCA the opportunity to revisit your complaint and put things right, which they declined. At this point I took the case on to undertake my own investigation.

Following a full file review it became apparent that the information which had been obtained by the Complaints Team to prepare their response to you had been insufficient to evidence their

findings, and was even contradictory in places. My follow-up questions were not addressed sufficiently and my requests for additional documentary evidence were not met.

At this stage, following a face-to-face meeting with senior staff at the FCA, it was agreed that my enquiries had not been handled correctly and that the responses provided were not adequate. It was agreed that a specialist Supervision team, independent of the team that were directly responsible for the supervision of the firms in question, would carry out an internal review of the supervisory work done in relation to the firms and assess whether this was sufficient or if there had been opportunities missed. The team were also tasked with providing a detailed chronology of events and a complete report setting out their views.

Action taken by the regulator – element one

Their work took some time to complete but was extensive and thorough. I am now going to provide a chronology of events to explain what work was undertaken and set out my view of it. I should emphasise that for confidentiality reasons I am unable to give very detailed information about the specifics of the work undertaken, but I wanted to demonstrate my findings to you.

Date	Event	Notes
August 2009	Treating Customers Fairly verification visit to Seymour Mullens (SM)	Satisfactory outcome – firm able to demonstrate good practices
September 2009	Portland takes over SM	
April 2010	Managing Investments (discretionary service) added to SM permissions.	
May 2010	Mr A resigns from SM.	
May 2011	First whistleblowing report received by the regulator.	
June 2011	Second whistleblowing report received by the regulator.	
June 2011	Supervision begins work in relation to the allegations made in the whistleblowing reports.	Supervision sought input from various internal departments, such as Enforcement and the General Counsel Division (GCD), as well as externally from the City of London Police (CoLP). A significant amount of work was undertaken to verify the information provided and to identify the best way forward to protect consumers and

		maintain the integrity of the market.
October 2011	The regulator conducted a firm visit and set out their findings and concerns in a letter to SM.	
November 2011	The regulator requests details of the firm's PII cover.	
December 2011	Mr A contacts the FCA with information.	
December 2011	Continuing work undertaken by the regulator to establish the firm's financial standing, how it would cover liabilities and what steps are available to the regulator under their powers (in relation to all the firms within the group).	
February 2012	Regulator requires SM and other group companies not to place further business in the UCISs.	
March 2012	Mr A talks to the regulator to aid their ongoing work.	At the same time, the firms are challenging the regulator's actions and plans for dealing with the issues identified, leading to distractions and delays.
March 2012	Mr and Mrs H become aware of the high-risk investments of their SIPPs, complain to SM and request that their investments are made moderate risk again, in line with their risk tolerance.	
April 2012	Further reports from individuals and other firms raising concerns about the group of firms already under investigation.	
May 2012	Work is continuing to be undertaken to establish the firms' ability to cover all liabilities and pay	

	compensation on complaints; contact is made with HMRC; assessment of the connections between the various firms within the group and the investment funds are being undertaken. Concerns about the lack of assets / funds within the UK firms for covering liabilities to consumers, should this become necessary.	
July 2012	Further contact with CoLP regarding the concerns about the group of firms.	
August 2012	SM applies to have all their permissions cancelled. Continuing work undertaken to establish the firms' plans, using statutory powers due to non-compliance. The aim is to ensure consumers are protected and past liabilities are met but serious concerns regarding their ability to meet their obligations. Mr and Mrs H complain to the FOS.	
October 2012	The regulator is exploring various avenues for preserving what little capital the firms have and ensuring that consumers are protected and aware of where they stand in relation to the firms. The firms continue to declare willingness to co-operate with the regulator but they are creating obstacles. The regulator is in contact with the police regarding the firms.	
December 2012	Mr and Mrs H's complaints are upheld by the FOS but	

	SM challenges the decision – referral to an Ombudsman.	
January 2013 – June 2013	Further work undertaken by the regulator in an attempt to secure an orderly wind-down of the firms and protect consumers but the firms stopped paying their regulatory fees and, as a result, SM's authorisation was withdrawn in June 2013.	
June 2013	Ombudsman upholds Mr and Mrs H's complaints.	

As can be seen from the above chronology, the regulator did act based on the whistleblowing reports it received and well before the first report from Mr A. The information Mr A provided was used in their work and they did seek further details from him directly. Various departments of the regulator worked together in an attempt to preserve funds for consumers. However, it appears that the group of firms in question had little tangible funds in the UK and used a number of legal means available to them to challenge and delay the work of the regulator. Even if the regulator suspects wrong-doing by firms, it must follow the correct procedure, which of course includes the right of reply for firms, in investigating and addressing the potential issues.

It seems to be the case that long standing and reputable financial services firms were used in order to be able to move trusting investors to discretionary management and invest their funds in high risk portfolios, which then, unfortunately, resulted in significant losses to the investors.

It is clear that a significant amount of work was undertaken by various departments of the regulator and attempts were made to protect consumers.

PII – element two

This element of your complaint focused on the issue that SM and/or P appeared not have had PII in place at the relevant times and for that reason, you as a consumer who lost money over the FSCS compensation limit, could not take advantage of this additional level of protection.

Investigating this element of your complaint also required significant input from my office. Following extensive enquiries with the regulator, I have seen evidence that confirms that SM did have PII in place while conducting regulated business. The regulator asserted in their response to your complaint and in their correspondence with my office that there was PII in place, but it was only with great difficulty that they were able to prove this was the case. It took several attempts for my office to obtain the required evidence and there seemed to have been confusion within the Complaints Team about the meaning of the information contained within the GABRIEL reports and whether there were other systems or methods used by firms for reporting on PII to the regulator.

This confusion could and should have been avoided by ensuring that the purpose of my questions and the information supplied to my office was understood before issuing a response.

However, it is now clear that SM and the other firms within the group did have valid PII at the relevant times.

The RMAR/GABRIEL returns flag up if PII details are not entered. However, it is not the usual process for the regulator to check every PII policy put in place by regulated firms, as trust is placed in them to secure the required level of cover.

In response to your comments to my preliminary decision, we have made further inquiries, and apologise for the fact that we did, regrettably, miss an element of the report prepared by the regulator, which is relevant to the PII point.

Having reviewed the terms of SM's policy, I see that it specifically excluded losses resulting from investments made under discretionary management and all losses related to investments made in the funds in question. Had SM complied with the terms of the insurance and reported any claims as they arose to their insurance providers, it appears that losses related to the funds your SIPP was invested in would still, unfortunately, not have been covered.

As stated above, while the Regulator does not routinely check the details of individual policies, it did become aware in December 2011 of the specific exclusions of the PII in place at SM. The firm was classified as a BIPRU 50k Euro limited licence firm and the regulator's approach to such firms is set out as *"we understand that there was no generic rule that would have required BIPRU firms to hold additional capital to cover exclusions on PI policies. We understand the FSA approach at the time for dealing with such exclusions would have been to consider on an individual firm basis taking account of a number of factors including the firm's regulated income, ICAAP and nature of the exclusion. If a need for additional capital to cover the exclusion was identified we would have expected a request to be made to the firm to inject additional capital to cover the exclusion. Where a firm failed to meet such a request, we would have expected immediate steps to require the firm to cease the activity related to the exclusion. We don't believe these actions would differ according to the product covered by the exclusion."*

The regulator went on to say that *"we found no evidence that the supervision team considered the need for additional capital when they were given notice of the exclusion in December 2011. We ..... believe this to be something Supervision should have considered."* I agree with this assessment: the failure to consider this point was a significant one.

The regulator also went on to state that they do not believe this failure would have caused significant consumer detriment in the two months between these exclusions coming to light and the firm signing a moratorium undertaking not to place further funds in these UCIS. The regulator also believes the firm would not have complied with a request to inject further capital into the business as the *"Supervision team asked the P Group to inject additional funds to address another capital deficit issue at SM in August 2012. The P Group responded stating that it was unlikely AS would make any further funds available as the Group was pulling out of the UK. As the P Group had signalled its intentions to wind-down, and cancel its permissions, in November 2011, we believe any request in December 2011 to inject additional funds to address a capital deficit at SM would have been met with a similar response to that given in August 2012".*

Had the firm failed to inject further capital, the regulator would have asked the firm to stop investing in the relevant funds in late December 2011 or early January 2012. The failure to consider whether further capital was required, therefore, meant SM was able to continue to invest client funds in the H and O funds between late December 2011 (when the Group advised of the exclusion on SM PII policy and when the regulator consider a requirement should have

been placed on SM permission to stop it carrying out discretionary management activities and advising on UCIS) and 12 February 2012, when the moratorium was signed. While the regulator failed to consider the exclusion point, I do not believe that, had they done so, the outcome would have been different for clients of these firms.

This clarification was provided by the regulator following your comments and I am sorry my investigator did not pick up on the significance of the matter in the first instance.

In your comments to my preliminary decision you go on to state *"the complaint against SM is for breach of contract, failure to disclose undeniable conflicts of interest (they invested his money in funds under their direct control, to the extent that they ultimately converted his investment into a loan to themselves - which is now ongoing and unlikely to be repaid) and failure to respect the agreed risk parameters… The FCA alone was in a position to ensure the client was protected and could and should have done so - they did not."*

I have carefully considered these points. First, I cannot make a judgement on poor treatment of customers by firms or breaches of contract: that is not within the remit of this Scheme.

Secondly, I have considered what would have happened, had the regulator considered and found that the firm needed to inject additional capital in light of the PII exclusions. Having seen extensive information about the firm's dealings with the regulator and its clients, it seems to me highly unlikely that they would have injected additional funds as requested. Unfortunately, even if the firm had complied, it is improbable that a moderate capital injection in December 2011 or January 2012 would have meant that your and other investors' losses would have been prevented.

I disagree with your assertion, made through your representative Mr A, that the regulator alone was in a position to ensure that consumers were protected and the terms of the existing PII were met. That was the responsibility of the firm. The firm had clearly acted in a way that was not in the best interest of consumers and appears not to have been open and honest with the regulator while claiming to be co-operating with it, when the regulator was taking steps in a bid to protect consumers, albeit not with much success.

In relation to the point you raise that PII would have covered your losses for breach of contract, failure to disclose undeniable conflicts of interest and failure to respect the agreed risk parameters, had the firm reported the existing complaints against them in line with the terms and conditions of their PII policy, it was not part of the process at that time for the regulator to verify that firms which applied to cancel their permissions had reported all existing claims to their insurance provider. I have already raised this issue with the regulator in an unrelated case and recommended that they incorporate this step into their checking processes, as part of approving a firm's application to cancel their authorisation, precisely to ensure that existing claims are reported correctly and consumers are afforded the highest level of protection. The regulator accepted this and has already made a change to their processes. You can find further details of this complaint here:

http://frccommissioner.org.uk/wp-content/uploads/FCA00181-FD-final-05-12-16.pdf

Conclusion

I uphold the regulator's decision to reject your complaint, because I have found that they took reasonable action in relation to the information they received from whistle-blowers regarding

P and its group companies, including SM, and they met their obligations in ensuring that authorised firms hold PII. Although they should have considered whether a capital injection would have been appropriate in December 2011, it seems to me highly unlikely that their failure to do so had any effect upon the losses which you suffered.

However, I find it very disappointing that there appeared to be an inadequate effort from the Complaints Team to fully understand your concerns and to get to the heart of the issue, and that my initial enquiries were met with such insufficient responses that it was necessary for my office to arrange meetings with senior staff at the FCA and for them to instigate an internal review. The process was prolonged and, as a result, it has taken me more than a year to be able to complete my review of your complaint. For their initial failings in dealing with your complaint and the following delays, I **recommend** that the FCA offer to pay you £1000 for distress and inconvenience.

I am sorry it has taken so long to complete my investigation and I am sorry that it has not produced the outcome you were hoping for. However, I hope you understand how I reached this conclusion, and have a clearer understanding of the sequence of events.

Yours sincerely,

Antony Townsend
Complaints Commissioner