

11 April 2022

**Final report by the Complaints Commissioner****Complaint number FCA001434***The complaint*

1. On 30 September 2021 you asked me to investigate a complaint against the FCA.

*What the complaint is about*

2. The FCA summarised your complaint as follows:

You are complaining about the accuracy of statements made by the FCA following the publication of the independent review on Connaught.

Specifically, you have alleged:

When the FCA announced the publication of the Connaught independent review on 17 December 2020, it incorrectly stated that when Connaught entered liquidation on 3 December 2012, the outstanding principal invested by investors was £79 million. You state this figure was actually £104 million.

The FCA's response to the independent review on Connaught gives the impression that investors have received all their funds back. However, you consider this is misleading because this figure does not take into consideration consequential losses, loss of income and opportunity costs.

When the FCA announced that Blue Gate Capital Limited (Blue Gate) had been ordered by the FCA to pay investors £203,007 in restitution, it set out the intention and broad terms of the payments made to investors following the £66 million payment from Capita Fund Managers (CFM). You consider the statement was untrue because it did not take into consideration consequential losses including the false presumption that sophisticated, advised clients would have invested in an illiquid

investment product generating almost zero returns for a period of approximately a decade.

You believe “the FCA’s actions in seeking to mislead the Treasury, politicians, the media and other stakeholders into believing, wrongly, that the Connaught victims are not still bearing material, unremedied losses therefore has the appearance of being a clumsy, bad-faith attempt to evade liability for those costs.

*What the regulator decided*

3. The FCA’s decision letter to your complaint is attached as Appendix 1 to this report. It did not uphold your complaint.

*Why you are unhappy with the regulator’s decision*

4. You have made the following points to me:
  - a. ‘The FCA made public statements in December 2020 implying them stating that investors in The Connaught Income Fund Series 1 had recouped all their invested capital and even been placed in the position they would have been in had they not invested in the Fund.
  - b. As an investor in the Fund and a member of its liquidators' committee, I knew those claims to be untrue, and I engaged promptly with the FCA's Chief Executive Nikhil Rathi seeking publication of a correction. None has been forthcoming.
  - c. The FCA claims its statements are truthful, but it does so solely by arguing that they rely on the same calculation as did its November 2017 statement announcing the payment of some voluntary redress by Capita. No investor or representative thereof (including the Fund's liquidators, or the liquidators' committee) has ever accepted that this statement represented an accurate calculation of investors' losses, and indeed under the Insolvency Act 1986 the FCA's calculation is plainly incorrect.
  - d. First, the FCA's statement relies on retrospectively reclassifying income received from the Fund as if it were returns of capital. Clearly, income and capital are neither interchangeable nor fungible; whatever its shortcomings, not even the FCA would allow authorised firms to pretend that one is the

same as the other, so the regulator cannot be allowed to pull that trick. The Fund's name - originally the Guaranteed Low-Risk Income Fund Series 1, subsequently the Connaught Income Fund Series 1 - and its regulated financial promotions all made it explicit that the distributions received during an investor's participation were of income; this was confirmed by the advice notes accompanying the quarterly distributions and in the investors' tax returns. The FCA's claims are built on the dishonest reclassification of income payments as receipts of capital. Reversing this confirms the FCA's statements are untruthful.

- e. Second, the 2000 or thereabouts individuals who invested in the Fund were required to pass the tests for high net worth or sophisticated or professional investor status applicable at the time, and to be professionally advised by authorised financial advisers; they also required a risk appetite that extended to UCIS funds. Against this background, it is clearly reasonable to expect that if they had not invested in the Fund, they would instead have put their money to work elsewhere, generating similar returns with the claimed liquidity or greater returns in products or assets as illiquid as the Fund turned out to be. It is unreasonable to suggest they would have kept their money in cash, and ridiculous to propose that they would do so but pay tax on a level of income substantially higher than that received - the two positions you would have to accept if you upheld the FCA's calculation.
- f. I note your [statement](#) dated 17 December 2020 that you are considering the contents of the Independent Review of the Fund. Parker concluded (par 16) that 'investors recouped a considerable proportion of their investment', a statement that implies that a proportion of their investment remains outstanding and is silent about the recouping of economic losses such as expected returns on that capital, or consequential losses or opportunity costs.
- g. You could help Connaught investors enormously by finding in favour of my complaint and recommending that the FCA corrects its statements and commences an investigation into the officers' conduct in making the misleading claims and failing to rectify them. I suspect that you doing so

would bring the regulator to the negotiating table to discuss the payment of long-overdue redress for the considerable shortfall that exists, causation of which is the failure to provide appropriate and effective regulation identified by Parker.

- h. It is self-evident that Connaught investors are bearing unremedied losses and I am prepared to put time and money into pursuing this, including judicial review of my complaint, if necessary. I believe that such scrutiny would expose the regulatory system to yet further reputational harm, and hope that you are able to persuade the FCA of the wisdom of instead accepting the inevitable, which includes admitting that I and my fellow investors are bearing unremedied losses caused by regulatory failure and engaging constructively with us about remediation.
- i. I have the permission of the Joint Liquidators to share with you their latest report that the limited partners (= investors) were owed c.£104m on appointment (which includes a small amount of interest, correctly calculated under Rule 14.22 of the Insolvency Rules 2016), and have since received distributions of c.£22m, indicating a shortfall of £82m from the insolvency process. In addition, investors benefited from the voluntary redress scheme negotiated by the FCA (I believe £56-57m; the FCA could confirm the exact quantum to you). It therefore follows that the shortfall on the capital account alone must be in the region of £25-26m.
- j. Additionally, you will be aware that under section 189(2) of the Insolvency Act, creditors are entitled to receive interest at the greater of eight percent per annum and any applicable contractual right (in the case of the Fund, between 8.15 and 8.50 percent per annum, depending on the quantum of capital subscribed by that investor, calculated quarterly - see attached information memorandum). This should be calculated on the outstanding amount of capital and accrued interest at each quarter date. For much of the relevant period the principal and accrued interest has exceeded the £104m owed on liquidation, and therefore even after the aforementioned distributions a liability far in excess of the £25-26m remains outstanding'.

### *Preliminary points*

5. On 17 December 2020 the FCA published the Independent Review of the Connaught Income Fund Series 1 (the Parker report)  
<https://www.fca.org.uk/publication/corporate/connaught-independent-review.pdf>.
6. This review is independent from my office and I am unable to review or investigate any of its findings. You have said to me that 'Parker concluded (par 16) that 'investors recouped a considerable proportion of their investment', a statement that implies that a proportion of their investment remains outstanding'. You have clarified that you have brought this to my attention as corroboration of your allegation that investors have not recouped their capital entirely. The Independent Review does not provide further clarity on this point and it is not certain on what basis it arrived at the conclusion that "investors recouped a considerable proportion of their investment'. Nor is it certain that the reference to investment in the Parker report is interchangeable with capital. You, on the other hand, have been clear as to the reasons you believe investors have not recouped their capital investment. I have reviewed the reasons you have presented on their own merit.

### *My analysis*

7. The FCA's decision letter (Appendix 1) explains that it has classified investor losses in Connaught Income Fund Series 1 (the Fund) in one of two ways: by referring to investors' losses excluding interest, redemptions, distributions, payments or dividends determined to be £79 million pounds and to losses including the latter determined to be £104 million pounds.
8. In December 2020 the FCA issued a response to the Report of the Independent Review into the FSA and FCA's handling of the Connaught Income Fund Series 1 and connected companies (the Parker report). In this response it said that 'The Fund entered liquidation in 2012, before we became the FCA, with aggregate principal losses estimated at £79m. Since then, investors have received over £80m, including over £58m of redress under the settlement we secured from Capita Financial Managers (CFM)'
9. You say this is untrue and you would like the FCA to publish a correction. You have given two main reasons above in support of your assertion:

- a. First because 'FCA's statement relies on retrospectively reclassifying income received from the Fund as if it were returns of capital'- 'The FCA's claims are built on the dishonest reclassification of income payments as receipts of capital'. And that 'Reversing this confirms the FCA's statements are untruthful'; and
  - b. Second, because the investors in the fund being high net worth and professional investors would have invested their money elsewhere if not Connaught for a similar return, and 'It is unreasonable to suggest they would have kept their money in cash'.
10. You have pointed out the FCA Blue Gate Final Notice 18 December 2020 – <https://www.fca.org.uk/publication/final-notice/blue-gate-capital-limited-2020.pdf> says that 'approximately £104 million of capital and interest was owed to Investors.' It is your view that this figure is more representative of the real amount owed to investors.
11. I have considered your arguments above and my view is that they are tantamount to a disagreement with the redress methodology calculation. I note you disagree with me on this point and have said that 'The FCA was entitled to enter into whatever agreement it wished with Capita in 2017 and to calculate redress however it wished', and that your complaint 'relates solely to the events of December 2020 in which the FCA misrepresented the redress secured under the abovementioned agreement'. You have said that the FCA is 'giving false and misleading impressions that the consequence [of the redress agreement] was to remedy all investor losses'. And that you do 'not accept that the FCA has any right to represent the sums received by investors under that scheme as having returned the totality of their capital'. The agreement which the FCA entered with Capita in 2017 was to return to the Fund's Investors their capital investments less any amounts which they had already received in interest and by way of redemptions, distributions, payments or dividends. As the FCA explained, 'the £79 million figure is in line with the Capita redress methodology and its intention to return investors as closely as possible back to the position they would have been in had they never invested in the Fund'. The proposed methodology did not guarantee that investors would be put back in that position, only that it would try to do so as closely (my emphasis) as possible. The FCA's

December 2020 statement that 'investors have received over £80m, including over £58m of redress under the settlement we secured from Capita Financial Managers (CFM)' does not say that all investor losses have been recovered or that the totality of all capital was returned to each and every investor. I will return to this point below.

12. You have argued that this alleged misrepresentation on the part of the FCA in referring to an aggregate Fund loss of £79 million is due to the FCA 'retrospectively reclassifying income received from the Fund as if it were returns of capital'. You disagree with this approach.
13. So, on the one hand, you say you do not disagree with the redress methodology and on the other hand you have told me that income received from the Fund should not be considered as a return of capital: yet this is precisely what the redress methodology says it will do. Your comment is as follows: 'The FCA was entitled to enter into the agreement with Capita and to calculate redress payments as it did; but income and capital are different things, so it must not misrepresent that deal as having returned 100% of investors capital when it is a matter of empirical fact that it did not.'
14. You have continued to press the point that that income payments cannot retrospectively be categorised as repayments of capital and that I am 'sitting on the fence' on this point. You have said to me 'Should you be in any doubt about the technical veracity about my specific point about income and capital or my broader argument that Connaught investors cannot truthfully be said to be in the position they would have been had they not invested in the Fund, I urge you to seek a relevantly qualified and independent (of the FCA) professional opinion on the matter; it will vindicate my position', and 'if capacity constraints have impaired your ability to conduct a proper investigation of my complaint, I hope you will secure appropriate external resource in order to remedy this'.
15. Although you claim you agree 'The FCA was entitled to enter into the agreement with Capita and to calculate redress payments as it did', it is evident from your arguments that de facto you disagree with the way the FCA and Capita agreed to calculate redress payments. This is because the 2017 agreement specified that its aim was to return capital investments less any

amounts which they had already received in interest and by way of redemptions, distributions, payments or dividends, whereas your point is that 'Capital and income are two different concepts; they are neither fungible nor interchangeable. A payment of interest is not a return of capital.' Therefore, your view is that investors have not had the totality of their capital returned based on your interpretation.

16. You have asked me to either agree with you on the technical point of whether a payment of interest is a return of capital, and if I cannot do that, to seek further advice on this point. I am afraid that it is not within the remit of the Complaint Scheme for me to provide legal or expert interpretations of financial meaning of such categories. But I do not think that anything turns on this technical point. The crux of the matter is that the FCA and Capita entered into a private agreement, within the discretion of the FCA, for a form of restitution to affected investors, and it specified a clear methodology of how this would be achieved: the return, as far as possible, of capital invested 'less any amounts which they had already received in interest and by way of redemptions, distributions, payments or dividends'.
17. In December 2020 the FCA published this statement in response to the Parker review: 'The Fund entered liquidation in 2012, before we became the FCA, with aggregate principal losses estimated at £79m. Since then, investors have received over £80m, including over £58m of redress under the settlement we secured from Capita Financial Managers (CFM)'.
18. The statement above does not claim, as you say, of 'having returned 100% of investors capital'. The FCA's position has always been that capital will be returned 'less any amounts which they had already received in interest and by way of redemptions, distributions, payments or dividends'.
19. You have also said to me 'The FCA's response to the independent review on Connaught gives the impression that investors have received all their funds back and that they have been left in the position they would have been had they not invested in the Fund'. You have pointed out to me that these investors, 'had they not invested in the Fund they would have invested in other products generating similar or greater returns'. I appreciate your point but the redress



methodology agreed between the FCA and Capita specifically excludes consequential loss.

20. I understand that you believe that redress for investors should be calculated based on £104 million (or more) based on investors principal losses as well as interest redemptions, distributions, payments or dividends and other payments such as 'expected returns on that capital, or consequential losses or opportunity costs', and continue to feel the reference to the sum of £79 million is flawed.
21. The FCA's final notice on Blue Gate (18 December 2020) gives the £104 million figure rather than the £79 million mentioned in its response to the Independent Review the day before. I agree with the FCA's explanation that 'Both the £79 million and £104 million are correct depending upon whether the contractual liabilities, in addition to the capital invested, is considered or not.' The crux of the matter is that the FCA and you have different opinions about which of these numbers should have been used as the amount outstanding for redress purposes as of 3rd December 2012 when Connaught entered liquidation.
22. Whilst I don't think it can be said that the statement in the FCA response to the Independent Review was inaccurate, untruthful or requires a correction, one might argue that a truly reflective regulator would have set out the position more completely, but I don't think the omission could be considered evidence of bad faith.
23. You have said you disagree with my view and you have also said that 'Moreover, we know that Enforcement spent several years investigating then proceeding against Blue Gate Capital Limited, something 'X' told me he would not do unless he believed there were material financial upsides for investors. He would not have sought such redress had he not believed, correctly, that they were still suffering unremedied losses. So, I would expect there to be evidence within the chronology of the FCA's interactions with Blue Gate, including its attempts to pursue that firm to a restitution end point, that are all supportive of my assertion that the FCA acknowledges privately that Connaught investors did not recover their initial capital and have not been placed in the position they would have been had they not invested in the Fund. I asked you to obtain and

review emails and other documents and if appropriate interview the relevant executives to establish the veracity of my claims in this regard.’

24. The crux of your argument above is that you allege the FCA privately agrees with you that ‘the investors did not recover their initial capital and have not been placed in the position they would have been had they not invested in the Fund’ and you would like me to find the evidence of this by reviewing ‘appropriate documents’ and interviewing ‘relevant executives’. The FCA has responded on this point that in the absence of the provision of any specific details this has not and would not be investigated any further and that during its review of the numerous documents in the complaint case it did not see any evidence to support this allegation. I have also not seen anything in the file provided to me from the FCA to support your allegations and I agree with the FCA’s position on this point that in the absence of specific evidence or details from you there are no grounds to pursue this point further. The FCA has been very explicit about defining the extent of the redress scheme, it has reported redress figures in line with its proposed methodology and I have concluded it has not been misleading in its presentation of information. Therefore, there is no grounds for further investigation on my part unless you are able to provide new evidence.
25. There are other matters which you initially complained to the FCA about, and issues which the FCA touches upon in its decision letter (such as delay in issuing a response to you). You have not brought these and this report focuses only on matters which you have referred to me above.

*My decision*

26. For the reasons given above, I do not uphold your complaint that the FCA made public statements in December 2020 which were misleading. Whilst I don’t think it can be said that the statement in the FCA response to the Independent Review was inaccurate, untruthful or requires a correction, one might argue that a truly reflective regulator would have set out the position more completely, but I don’t think the omission could be considered evidence of bad faith.

Amerdeep Somal

FCA001434

Complaints Commissioner

11 April 2022