



23rd January 2012

Dear Complainant,

**Complaint against the Financial Services Authority
Reference Numbers: GE-L01363**

I write with reference to your email of 6th December 2011 in relation to your complaint against the Financial Services Authority (FSA).

At this stage, I think it would be worth explaining my role and powers. I am charged, under Paragraph 7 of Schedule 1 of the Financial Services and Markets Act 2000 (the Act), with the task of investigating those complaints made about the way the FSA has itself carried out its own investigation of a complaint that comes within the complaints scheme. The investigations I undertake are conducted under the rules of the Complaints Scheme (Complaints against the FSA - known as COAF). I have no power to enforce any decision or action upon the FSA. My power is limited to setting out my position on a complaint based on its merits and then, if I deem it necessary, I can make recommendations to the FSA. Such recommendations are not binding on the FSA and the FSA is at liberty not to accept them. Full details of Complaint Scheme can be found on the internet at the following website; <http://fsahandbook.info/FSA/html/handbook/COAF>.

Your Complaint

From your correspondence with my office, I understand that your complaint relates to the following:

1. You allege that the FSA failed in its statutory duty to protect individuals who engaged the services of an authorised firm.
2. You allege that the FSA's supervision of your financial adviser was inadequate. To support this allegation you have highlighted the firm's poor record keeping and working practices (which you refer to as poor and unusual). You also add that as a result of the FSA's failure to supervise adequately the firm, you have lost a considerable amount of money and are looking for the FSA to correct this by way of a compensatory payment.

Coverage and Scope of the Scheme

COAF provides as follows:

- (1) The complaints scheme provides a procedure for enquiring into and, if necessary, addressing allegations of misconduct by the FSA arising from the way in which it has carried out or failed to carry out its functions. The complaints scheme covers complaints about the way in which the FSA has acted or omitted to act, including complaints alleging:
 - (a) mistakes and lack of care;
 - (b) unreasonable delay;
 - (c) unprofessional behaviour;
 - (d) bias; and
 - (e) lack of integrity.
- (2) [deleted]
- (3) To be eligible to make a complaint under the complaints scheme, a person (see COAF 1.2.1G) must be seeking a remedy (which for this purpose may include an apology, see COAF 1.5.5G) in respect of some inconvenience, distress or loss which the person has suffered as a result of being directly affected by the FSA's actions or inaction.

I should also make reference to the fact that my powers derived as they are, from statute contain certain limitations in the important area of financial compensation. The Act stipulates in Schedule One that the FSA is exempt from "liability in damages". It states:

- "(1) Neither the Authority nor any person who is, or is acting as, a member, officer or member of staff of the Authority is to be liable in damages for anything done or omitted in the discharge, or purported discharge, of the Authority's functions.*
- (2) (Irrelevant to this issue under investigation)*
- (3) Neither subparagraph (1) nor subparagraph (2) applies*
 - (a) if the act or omission is shown to have been in bad faith; or*
 - (b) so as to prevent an award of damages made in respect of an act or omission on the ground that the act or omission was unlawful as a result of section 6(1) of the [1998 c.42] Human Rights Act 1998."*

COAF nevertheless then goes on to provide in paragraph 1.5.5 that:

"Remedying a well founded complaint may include offering the complainant an apology, taking steps to rectify an error or, if appropriate, the offer of a compensatory payment on an ex-gratia basis. If the FSA decides not to uphold a complaint, it will give its reasons for doing so to the complainant, and will inform the complainant of his right to ask the Complaints Commissioner to review the FSA's decision."

If I find your complaint justified, it is to that paragraph that I must refer in order to decide any question of a "compensatory payment on an *ex-gratia* basis". I formally record at this point given the above statutory provisions that I have found no evidence of bad faith nor have you suggested that the FSA has been guilty of bad faith on its part.

If you were to take the view that Schedule One referred to above was relevant in the context of the Human Rights Act 1998 I should explain that Section 6(1) of that Act that is referred to, provides as follows:

“It is unlawful for a public authority to act in a way which is incompatible with a Convention right”.

The only Convention rights that I consider may be relevant are contained in Article 1 of the First Protocol set out in the Human Rights Act of 1998.

Article 1 of the First Protocol provides:

“Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties”.

It is my view, given my views in this matter, that Article 1 of the First Protocol has no application in your case.

My Position

I have now had the opportunity to review the papers both you and the FSA have presented to me. From these papers it appears, understandably, that you are unhappy that you have lost money as a result of the investments you made through your financial adviser. I would add that, whilst you say that the financial adviser’s recording keeping was poor and it had, what you describe as, unusual working practices, and as a result claim that the poor supervision of the firm has led to your losses, I note that you have not provided any evidence to support this assertion in order to show that the losses you say you have incurred were the *direct result* (my emphasis) of the alleged regulator’s failures rather than the result of poor investment performance (which you describe as mis-management).

As I am sure that you are aware, the role of a financial adviser is to recommend a product which meets the consumer’s financial objectives. Any recommendation the financial adviser makes will be based upon a number of factors which may include (but will not be limited to) the consumer’s aims and objectives, the provider which offers a generic (or bespoke) product which allows the consumer to meet these aims and objectives, the consumer’s age, the consumers attitude to risk and what the adviser believes to be the most appropriate funds given the consumers other investments.

Whilst a financial adviser may recommend a product which meets these generic requirements, a number of factors can influence how a product and underlying investment fund(s) perform. Unfortunately here, as a matter of course, I must point out that the use of a financial adviser to make an investment does *not guarantee* (my emphasis) that investment decisions will result in a gain or profit for the investor. The outcome generally depends on the acumen of the adviser and there is a vast range of ability in that particular area as is indicated by the overall performance of the entirety of his duties by your financial adviser.

I can and do understand why are unhappy and appreciate that you say you have lost a considerable amount of money as a result of, what you describe, as poor recommendations and the poor management of your investments by the firm.

From the information presented to me, I understand that your pension arrangements, albeit recommended by your financial adviser, were managed by professional fund managers working for asset managers and *not* (my emphasis) by your financial adviser himself. As such, from the limited information presented to me, it does not appear that the losses you say you incurred necessarily resulted from the direct poor management of your investment by your financial adviser as opposed to the general economic climate in the context of the professional fund managers used and how they performed.

I now come to your comments about the supervision of the firm. The FSA has pointed out in its decision letter that it regulates approximately 27,000 firms, many of which are small organisations having a small number of employees (and/or advisers). Given that the FSA is funded solely by the financial services industry and not the government the FSA has to be mindful of how it uses its resources. As it would clearly not be possible for the FSA (under its current funding structure) to appoint a designated supervisor to each of the 27,000 authorised firms, the FSA has to adopt an approach which allows it to monitor the activities of all of the 27,000 firms and target its resources at the firms which pose the highest risk to consumers. This effectively amounts to risk based regulation which is the approach used by the majority of regulators

Under the Act, the FSA is given a wide degree of discretion concerning how it carries out its four statutory objectives which are:

- market confidence – maintaining confidence in the UK financial system;
- financial stability - contributing to the protection and enhancement of stability of the UK financial system
- consumer protection - securing the appropriate degree of protection for consumers; and
- the reduction of financial crime - reducing the extent to which it is possible for a regulated business to be used for a purpose connected with financial crime.

Given the FSA's statutory objectives, the number of firms which it regulates and the limited resources it has, the FSA has adopted a risk based approach to regulation. As such, the FSA requires all regulated firms to provide it with specific information (on a set report) on the firms' activities on a regular basis. The FSA reviews this information together and assess this together with any information it receives from consumers and that which it may obtains as a result of a periodic inspection visits carried out on the firms.

From the information presented to me it appears that based on the information the FSA held, your financial adviser was deemed to be what was described as a 'low impact firm'. As such, it was not being specifically monitored by the FSA and was supervised and monitored by the FSA's Small Firms and Contact Division and, given the low risk it posed, did not have a specific or designated supervisor (although as I have indicated above the firm's activities were monitored by the FSA).

I appreciate that you are unhappy that the FSA, when considering your complaint, would not provide you with further information relating to the specific interactions it has had with the firm in relation what you describe as the firm's poor record keeping and unusual working practices. Whilst I can understand why you are disappointed with the FSA's comments in relation to this, I must, however, in fairness to the gravamen of your complaint, now go into more detail. My starting point must be the Act itself. Section 2 of the Act sets out the FSA's general duties in the following manner:

- (1) In discharging its general functions the Authority must, so far as is reasonably possible, act in a way—
 - (a) which is compatible with the regulatory objectives; and
 - (b) which the Authority considers most appropriate for the purpose of meeting those objectives.
- (2) The regulatory objectives are -
 - (a) market confidence;
 - (b) public awareness;
 - (c) the protection of consumers; and
 - (d) the reduction of financial crime.
- (3) In discharging its general functions the Authority must have regard to—
 - (a) the need to use its resources in the most efficient and economic way;
 - (b) the responsibilities of those who manage the affairs of authorised persons;
 - (c) the principle that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction;
 - (d) The desirability of facilitating innovation in connection with regulated activities;
 - (e) the international character of financial services and markets and the desirability of maintaining the competitive position of the United Kingdom;
 - (f) the need to minimise the adverse effects on competition that may arise from anything done in the discharge of those functions;
 - (g) the desirability of facilitating competition between those who are subject to any form of regulation by the Authority.
- (4) The Authority's general functions are—
 - (a) its function of making rules under this Act (considered as a whole);

- (b) its function of preparing and issuing codes under this Act (considered as a whole);
- (c) its functions in relation to the giving of general guidance (considered as a whole); and
- (d) its function of determining the general policy and principles by reference to which it performs particular functions.

(5) "General guidance" has the meaning given in section 158(5).

From this you will see that, although the Act requires the FSA to discharge its regulatory objectives, it gives it discretion over how it does this providing that its act in a way which:

- (a) is compatible with the regulatory objectives; and
- (b) the Authority considers most appropriate for the purpose of meeting those objectives.

The composite effect of these provisions is to create an inevitable tension between market confidence, through the exercise of the FSA's regulatory powers and the protection of consumers. In effect the FSA has to balance sensitivity and careful judgement with the statutory requirements of all of its regulatory objectives. Issues like the ones raised in your complaint therefore will inevitably involve a consideration of difficult and differing courses of action for any regulator when seeking to deal both with prudential regulation and consumer protection. That is the generic background to the issues raised by your complaint.

It is clear from your correspondence with both the FSA and my office that you hold the FSA at least partially responsible for the investment recommendations the adviser made to you. You base this on the fact that you say that the adviser failed to comply with the established 'know your client' rules (as he failed to establish fully your attitude to risk or provide you with a 'recommendation letter' and indicate to you full details of the charges associated with the advice). You add that, in your opinion, had the firm been adequately supervised by the FSA, these failures would have been clear.

When supervising a firm, the FSA is unable to oversee and examine each and every interaction (such as the provision of advice) a firm may have with a consumer. Instead, as I have indicated above, the FSA adopts a risk based approach to regulation targeting its resources at the firms which pose the highest risk to consumers. Given the number of firms the FSA regulates, this is not an unreasonable position for it to take. If you feel that you received incorrect advice, then there are ways to raise this which I will come to later in this, my Final Decision.

Whilst the firm did not have a specific supervisor, as I have mentioned above, the firm's activities were monitored by the FSA. The FSA has explained in detail that its relationship with firms is confidential and section 348 of the Act prevents the FSA, or me, from making further comments about the nature of the interactions the FSA had with your financial adviser both prior to and since it was placed into administration.

I appreciate from your letter that you believe that the FSA is hiding behind section 348 of the Act as it will not comment upon the dealings but this is not the case. I know that you feel that this is an unattractive position for the FSA to adopt and feel that "*complaints in professions such as the law or medicine would be dealt with in a totally transparent and open manner and a response [which did not clarify what the regulator did] would not be tolerated*".

Although I can understand your considerable displeasure at the FSA's decision not to provide you with full details of the manner it supervised the firm concerned, ultimately, the FSA, like me, is simply prevented from making any further disclosure by section 348 of the Act. Although I can fully accept that it is quite reasonable for you (as the complainant) to pose the question relevant to this issue "well what exactly did the Regulator do to safeguard my interests as a consumer?" In answering those questions however, as I have explained above, *Parliament* (my emphasis) has imposed restrictions upon both the FSA and myself by the imposition of section 348 of the Act as to how those questions can be answered in the case of a complainant. Given that the relevant legislation is currently under review it may be that Parliament will revisit this issue.

In summary, *Parliament* (my emphasis) by virtue of Section 348 of the Act imposes upon the FSA, as the regulator, a ruling of confidentiality in the context of disclosing its response or position when acting in the discharge of its function as the relevant regulator. This means that, other than in limited circumstances, the FSA is unable to disclose any information about what action it did or did not take against a firm or individual (and the reasons for that decision).

In this instance, as I do not believe that the exceptions apply, I cannot comment in great detail, on the FSA's 'dealings' with the firms concerned. However, I do myself have the power to delve more deeply into such matters, in my role as Complaints Commissioner, to enable me to be satisfied as to the propriety of what the FSA has done. However, as I have indicated above, I am limited, in most cases, as to the further disclosure of the details that I am informed about. I am therefore unable, directly, to answer the questions you have posed.

As part of my investigation into your complaint I have however asked the FSA to provide me with the information relating to what action, if any, it took or may be taking in relation to the issue which lies at the heart of your complaint and the reasons for any decisions it may or may not have made. Although I am unable to comment on the information it has provided to me in great detail, in my view, I consider that at the time, the FSA took all appropriate steps relevant to the issue. However, I will, at this point, respond to the comment you made in response to my Preliminary Decision regarding the FSA requiring the firm to appoint an external compliance consultant. Although I cannot provide specific or further details in relation to this, what I can say is that the FSA did impose this requirement on the firm and that FSA decision to impose this requirement appears to have resulted from its general supervision of the firm.

The position therefore is that I have obtained freely from the FSA the appropriate information that the FSA exercised and made its judgements regarding the supervision of the firm on a reasonable basis. Whilst I appreciate why you hold the FSA at least partly responsible for the losses you say you have incurred, you have not, in my opinion, provided sufficient, if any, evidence to show that the losses you have experienced were the direct result of failure by the FSA to supervise adequately the firm *rather than* (my emphasis) the provision by the firm of either incorrect advice or that the losses are simply the result of the selection of badly performing investment funds by either you and/or your financial adviser.

I would add here that, as my role is to consider the actions (or inactions) of the FSA, I have not considered whether the losses you say you have incurred are as a result of adverse market movements (resulting from the current uncertain financial climate) or as a result of your financial adviser providing you with what could amount to unsuitable advice.

Whilst you have highlighted that the firm's record keeping was poor this, on its own, does not mean that the losses you say you have incurred were directly attributable to the recommendations the adviser made. Likewise, I appreciate that you have indicated that the FSA's inadequate supervision resulted in these losses, you have not provided sufficient, if any, evidence to show that this was the case. I would add here that, in my opinion, the information you have provided in response to my Preliminary Decision only supports a complaint of poor service and or advice on the part of the financial adviser rather than inadequate supervision on the part of the FSA.

In this instance, if you feel that the advice your financial adviser gave you was incorrect, you should refer the matter to the Financial Services Compensation Scheme (FSCS). The FSCS is the correct body to consider a complaint concerning the provision of incorrect advice by a firm which is no longer trading and/or has been placed into administration.

As I have indicated above, from the information available to me there is insufficient, if anything, to indicate that the FSA's supervision of the firm directly led to the losses you say you have incurred. I would add here for the avoidance of doubt that I am satisfied that the FSA's supervision of your financial adviser was adequate in all of the circumstances prior to the financial adviser being placed in administration. Likewise, whilst you say the losses you have incurred are the result of the FSA's inactions, from the limited information I hold, I believe that these losses could equally have resulted from the prevailing economic conditions or simply from the fact that you were incorrectly advised by your adviser. I appreciate that you say that your financial adviser is now in administration and no longer trading and, as a result, if you feel that you were given unsuitable advice you should refer your complaint about this issue to the FSCS which can be contacted as follows:

Financial Services Compensation Scheme
7th floor
Lloyds Chambers
Portsoken Street
London
E1 8BN

Telephone: 0800 678 1100 or 0207 741 4100
Fax: 020 7892 7301
Email: enquiries@fscs.org.uk

I would also add that whilst it is unfortunate that the firm has been placed into administration this does not automatically mean that the FSA's supervision of the firm has been inadequate. Financial advisers are, in effect, a business which needs to generate an income which is greater than the firm's expenses.

A financial adviser usually generates income from its dealings with consumers; this is usually either by way of commission (paid by a provider following the generation of a policy) or by fees (paid by a consumer for the provision of advice). Likewise, a financial adviser will have expenditure which has to be paid (which will result from items such as the costs of its premises and its staffing costs). It is unfortunate, but when any business is, for whatever reason, unable to meet its liabilities, it could be placed into administration. In the case of a financial adviser, the fact that the firm is regulated by the FSA does not mean that the firm cannot fail if its liabilities exceed its income for a period of time.

It is unfortunate that your financial adviser was placed into administration (and as a result you no longer have recourse to the Financial Ombudsman Service). However, as I have set out above, this is not automatically an indication of poor supervision on the part of the FSA. I would add here that, other than the assertion you have made, you have not provided any evidence to show that the placing in administration of your financial adviser was the *direct result* (my emphasis) of the alleged inadequate supervision of the firm by the FSA.

I can appreciate that all this is not the kind of answer you will wish to receive but it represents the position as I see it having regard to what I have established following my investigation. As such, I am unable to alter the decision from that which the FSA set out in its decision letter of 17th November 2011.

Finally, you may already know that the Government recently published a White Paper in a Draft Bill to amend the Act in a number of aspects. Section 348 will be replicated in the new legislation as it goes through Parliament but you may wish to approach your Member of Parliament about your case and the issue of section 348 and its application in your case.

Yours sincerely



Sir Anthony Holland
Complaints Commissioner