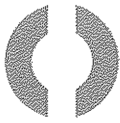

Complaints Commissioner

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FINAL DECISION

1. Background

1.1 Under Paragraphs 7 and 8 of Schedule 1 to the Financial Services and Markets Act 2000 (the Act), the Financial Services Authority (FSA) is required to maintain a complaints scheme for the investigation of complaints arising in connection with the exercise of, or failure to exercise, any of its functions under the Act other than its legislative function. The complaints scheme must be designed so that, as far as reasonably practicable, complaints are investigated quickly.

1.2 The implication of that provision is that the design of the scheme is fit for purpose, which I believe it to be, and has, so far as is practicable, features such that the complaints design should not impair or slow down the entire process of complaints investigation. Finally, the complaints scheme provides that an independent person is appointed as Complaints Commissioner with the task of investigating those complaints made about the way the FSA has itself carried out its own investigation of a complaint. The appointment has to be approved by H.M. Treasury. I currently hold that role.

1.3 The complaints scheme goes onto provide that there are two distinct stages which I hereafter refer to as Stage One and Stage Two.

1.4 Stage One is the investigation carried out by the FSA itself and Stage Two is the investigation that I carry out when the complainant is dissatisfied with the outcome of Stage One or where the FSA has refused to carry out the Stage One process.

1.5 The Stage Two 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. It is rare for the FSA not to accept any recommendation that I may make. Full details of Complaint Scheme can be found on the internet at the following website; http://fsahandbook.info/FSA/html/handbook/COAF.

2. The Complaint

2.1 Under paragraph 1.4.1 of COAF the complaints scheme provides a way of reviewing the FSA's actions and, if necessary addressing allegations of misconduct in the manner on which it has carried out, or has failed to carry out, its regulatory functions. The complainants in this case on whose behalf you have contacted me are unhappy with the FSA's actions and the outcome of the FSA's own investigation into his complaint. I have been asked to review the FSA's actions in accordance with the rules of the complaints scheme.

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2.2 In your correspondence with the FSA and my office you have set out your complaint in considerable detail. Although I have considered all of the points you have raised, I believe that your complaint can at this stage, in effect, be summarised under the following three headings:

2.3 **The FSA has failed to protect adequately consumers who invested/purchased Permanent Interest Bearing Shares issued by the Society A.**

Whilst you made a number of allegations/representations under this area ultimately you allege that the FSA did not protect adequately those consumers who purchased Permanent Interest Bearing Shares (PIBS) in Society A, which were later converted to Unsecured Perpetual Subordinated Debt Bonds (PSD) when Society A demutualised to become Firm A plc (Firm A) which was part of the Governor and Company of the Bank B (Bank B) and merged with Bank B's existing UK operation.

The FSA succinctly set out in its Stage One decision exactly what PIBS are when it stated:

"*In 1991 Society A issued £75m of 13.375% PIBS. PIBS are a perpetual capital instrument issued by a building societies and which carry the risk attached to such instruments, namely that their tradeable value could go up as well as down, they ranked below creditors and depositors in the event of insolvency and they were not covered by the investor protection scheme (either the Financial Services Compensation Scheme (the FSCS) or its predecessor). The PIBS were listed on the London Stock Exchange*".

You feel that as the PIBS were predominately purchased by elderly retail investors the FSA has a duty to ensure that the consumers who invested in the PIBS are treated fairly by the issuer. You add that the FSA has failed to regulate adequately the retail bond sector and say there "*are hundreds of thousands of individual UK retail investors who hold UK listed retail bonds acquired directly and not through a financial adviser. Retail investors should accept the consequences of the risks of direct investment in UK listed retail bonds. However they should be afforded regulatory UK regulatory protection (sic) from unfair and illegal treatment by issuers especially in the event of coercive offers where there is a financial disadvantage of being excluded from or otherwise unable to participate. The costs of challenging an issuer through the courts would run into hundreds of thousands of pounds plus the risk of adverse costs. Therefore it is not feasible for individual retail investors*".

2.4 **The FSA failed in its statutory requirements as the UK's Listing Authority when approving the 2007 prospectus issued by Firm A to change the issuer to Bank B.**

In 1997 the Society A was brought by Bank B and became Firm A, a wholly owned subsidiary of Bank B. At this time the PIBS were converted to 13.375% PSD as PIBS are a Building Society instrument that cannot exist on a plc balance sheet. As a result of this the issuer of the instrument became a wholly owned subsidiary of an Irish bank. The PSD are also subordinated capital instruments and carry the risk attached to such instruments. In 2005 Firm A sold its savings balances and branches to the Building Society C but the PSDs remained on the residual balance sheet of Firm A.

In 2007 Firm A's residual balance sheet transferred to Bank B (the Irish domiciled bank) and Firm A surrendered its banking licence. Bank B became the issuer of the bonds as part of a transfer of business (the Part VII transfer) sanctioned by the High Court. As part of this process Bank B produced a prospectus, approved by the UK Listing Authority (UKLA). This meant that there was no longer an FSA authorised subsidiary of Bank B in the UK.

In 2011 Bank B announced a debt for cash/equity swap as part of a Liability management Exercise which was part of the recapitalisation that Bank B was required to undertake by the Irish authorities. Holders of the 13.375% PSD were offered 20% in cash compensation or 40% in value of equity shares. This exchange offer was terminated but the firm stated its intention to instigate a new offer at a future date. Subsequently in 2011 Bank B made a cash only offer to bondholders worth c. 40% of the face value of the bonds, and approximately 39% of bondholders took up the offer. Ultimately, in 2011 the Irish Minister of Finance confirmed that, as Bank B had raised the required funding in their Liability management Exercise, he was currently not considering a Subordinated Liabilities Order in relation to the bonds.

You are now complaining on behalf of numerous small investors who hold/held 13.375% PSDs. Specifically you also allege that the FSA failed it is duties to assess correctly Firm A's 2007 prospectus (the 2007 Prospectus) which alerted PSD holders to Bank B's intention to transfer the issuer of the PSD from the Firm A to Bank B. You say that the 2007 Prospectus was defective as, *inter alia*, it gave a misleading impression of the effect of the scheme and that a winding up petition could be commenced in the UK when, under the terms of the transfer this would have to be carried out in Ireland. You also allege that the 2007 Prospectus was not in a form which was comprehensible and easy to analyse and wrongly stated that the bonds were governed by English Law when they were in fact governed by Irish Law.

2.5 **The FSA failed to stop Bank B from making a coercive offer to the holders of PSD which resulted in a number of them disposing of their holdings at a considerable loss.**

Specifically you say that the FSA, in June 2011, failed to consider the holders of PSD by allowing Bank B to issue a coercive offer which, in your opinion, did not give PSD holders sufficient time to consider their options and in so doing take appropriate advice.

3. The Complaints Scheme

3.1 COAF (1.4.1) 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.

3.2 I should also make reference to the fact that my powers derived as they are, from statute contain certain important 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."

3.3 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."

3.4 If I find your complaint justified, it is to that paragraph that I must refer in order to decide any question of a remedy including an award of a "*compensatory payment on an ex-gratia basis*".

3.5 If I 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 the Human Rights Act 1998 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".

3.6 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. 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.

3.7 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".

4. My findings.

4.1 I have now had the opportunity to review the FSA's investigation files and the submissions to this office. I have also had the opportunity to consider the additional information put to me.

4.2 Before commenting further I feel I must comment upon the unfortunate contact my office received from a journalist on 16th November 2012. As I set out at 1.7 above, until such time as I have issued and published my Final Decision, all correspondence between my office and a complaint must remain confidential save for situations where the complainant seeks legal advice on issues related to the complaint (although in this situation the complainant's legal adviser is then subject to the same confidentiality restriction as the complainant himself). This is confirmed by, paragraph 1.5.18A of the complaints scheme which states:

"The Complaints Commissioner expects his communications with complainants and the FSA during the course of an investigation to remain strictly confidential. Where a complainant breaches this requirement the Complaints Commissioner may, after having considered all the circumstances including any explanation from the complainant, decide to bring the investigation to an end without having to report under COAF 1.5.19G".

4.3. In this situation the journalist was clearly aware of the issue and was also fully aware of the nature of the complaint which had been passed to my office. I appreciate that you have assured me that you did not specifically discuss your complaint with the journalist concerned. However, whilst you may not have directly or specifically discussed the matter with her you clearly provided her with details of your complaint which allowed her to contact my office and ask for my Senior Investigator by name and then ask him questions which specifically related to the complaint which was submitted to my office. I find extremely unhelpful for any complainant to discuss an on-going complaint with any journalist.

4.4 As I have indicated above, paragraph 1.5.18A of COAF allows me to terminate my investigation without coming to a firm conclusion on the merits of your complaint. However, given the assurances you have given me, despite the fact that my office was contacted by a journalist who was clearly aware of the full nature of the complaint you had submitted to my office, I will not now invoke the terms of paragraph 1.5.18A of COAF and will therefore issue you with my Final Decision.

4.5 In your correspondence you have indicated that the FSA has not taken sufficient steps to protect the retail investors who hold or held PSDs which were issue originally issued as PIBS by Society A. In considering this point I feel that I should reiterate an explanation which was provided by the FSA. Whilst it is accepted that the PIBS were, and the PSD still are, held by retail investors, neither PIBS nor PSDs are retail investments. PIBS and PSDs are traded on the markets in a similar manner to shares. Additionally, like shareholders, holders of PIBS and PSDs are not offered any protection by the FSCS in the event of the failure of the issuer. Those purchasing retail investments usually will have recourse to the FSCS in the event of the failure of the issuer (or provider) or indeed if an adviser was involved.

4.6 Whilst you indicate that the holders of the PSDs which were originally issued as PIBS by Society A are mainly elderly retail investors, this is not a relevant point in relation to the manner in which bonds of this nature are issued. PIBS and PSD are in effect a type of corporate bond which is issued by an institution to allow it to raise additional funds from investors in return for an above average return. These bonds are offered to the market and 'purchased' by investors either on an execution only or advised basis.

4.7 If the holder of the bond believes at a future date that the bond was, in effect, unsuitable then the manner in which the bond was sold is relevant. If the holder was advised to purchase the bond by a financial adviser then the suitability of the advice can be challenged with the adviser and/or through the Financial Ombudsman Service (FOS). However, if the bond was selected by the holder with out advice (i.e. on an execution only basis) then the holder does not have recourse to the FOS as the investor must take responsibility for his or her own investment decisions.

4.8 I appreciate that you feel that the FSA should have introduced sufficient rules to protect retail investors, and have set out your views on this is considerable detail. However, the introduction of rules is not something which I can consider under the rules of the complaints scheme. I would specifically draw your attention to paragraph 1.4.2(3) of COAF which states:

1.4.2 <u>Exclusions from the Scheme</u>

Each of the following is excluded from the *complaints scheme*:

(4) complaints in relation to the performance of the *FSA's* legislative functions under the *Act* (including making *rules* and issuing codes and general *guidance*).

4.9 Unfortunately, the introduction of the rules you require falls under the FSA's legislative function. Whilst I can understand why you feel that rules such as those you have suggested are required I am simply not able to consider the FSA's actions in this regard nor make any further comment. What I would say is that the Prospectus Directive provides certain definitions and guidance as to what is required. Specifically it sets out the minimum disclosure requirements which must be included in a "prospectus" and that any individual who purchases securities through a prospectus is classed as an "investor".

4.10 However, that is not the end of the matter. When considering this, attention must also be paid to the definitions set out with in the Act itself. The Act sets out that an individual, who purchases securities *directly* (my emphasis) from a prospectus, is not an investor as they have not used the services of an authorised entity to purchase those securities (as they have acted in an execution only capacity). On this basis, whilst a regulated entity such as bank or building society may issues securities through a prospectus, individuals which purchase the securities directly through the prospectus (i.e. on an execution only basis) are not consumers of the bank; they would only become consumers of the bank if they used the services of the bank to purchase the securities (i.e. if they received financial advice about the securities from the bank itself).

4.11 As such, I would add that, in my opinion, shares and corporate debt (including PIBS and PSDs) are not retail investments unless the consumer has received specific financial advice about the security (and then the consumer would have the right to complain to the entity which provided the financial advice). I continue hold the view as such investments are not generally marketed by financial advisers to retail investors. Whilst many companies issue such bonds, they are in effect a specialist investment vehicle carrying a large degree of risk (where investors are compensated for the additional risk by receiving a higher level of income) and often requiring a large investment and are generally not suitable for unsophisticated retail investors particularly the kind you identify as "*elderly retail investors*".

Financial advisers do not usually recommend such investments to unsophisticated retail investors (other than as 'corporate bond' funds within a collective investment scheme which are packaged products managed by a specialist fund manager to mitigate some of the risks involved). Whilst it is clear that many were 'sold' to individuals who were savers with Society A this does not mean that they are retail investments as it is the nature of the actual investment rather than the nature of the holder which decides whether or not an investment is a retail investment.

4.12 In your response to my Preliminary Decision, you commented that you disagreed with my view that shares and corporate debt (including PIBS and PSDs) are not retail investments. In challenging my view you have referred to the FSA published "*Listing and Offers of Retail Debt in London - A Practitioner's Guide*" which highlights that the Prospectus Directive distinguishes between the minimum denominations for retail investments are less than €50,000. Given that the PIBS (now PSDs) were issued in denominations of £1,000 (which are therefore less than €50,000) you feel these should be considered as retail investments. Additionally you also add that "*2010 the London Stock Exchange established the Order Book for Retail Bonds (ORB) which is specifically designed to enable companies to issue new bonds directly to retail investors. Such issues are widely promoted in the mainstream press and through execution only stockbrokers to retail clients*".

Whilst I can understand how you have arrived at your view your comments have not persuaded me that my views are incorrect and I am still of the view that shares and corporate debt are not generally retail investments. Indeed, if I was to accept your view then virtually every share which was traded on the stock exchange would amount to a retail investment. Clearly this is not the case.

I would also add that whilst the FSA published "*Listing and Offers of Retail Debt in London - A Practitioner's Guide*" is simply a guide produced by the UKLA to help issuers and lawyers to produce a prospectus. The retail Debt Guide contains all the rules from the Prospectus Rules, Listing Rules and Disclosure and Transparency Rules that are applicable to Retail Debt Securities. Put simply the Retail Debt Guide contains extracts from the Prospectus Rules, Listing Rules and Disclosure and Transparency Rules that are applicable to retail debt securities and presents them in one booklet. The purpose of the guide was to have all the rules applicable to retail debt securities in one place and does not necessarily mean that just because the denominations of the securities were less than €50,000 they are classed as retail investments. I would also add that the relevant EEC Directive (80/390/EEC) *which was in force at the time of the issue of the PIBS* (my emphasis) does not provide an indication of what is or is not a retail investment. As such there is nothing to indicate that PIBS (or indeed PSDs) were retail investments.

Although I accept that the Prospectus Directive, enforced in the UK under the Prospectus Regulations 2005 (as a result of the subsequent amendments Directive 2003/71/EC made to EC Directive 2001/34/EC and EEC Directive 80/390/EEC), introduced a requirement of added protection for denominations of less than €50,000 it is unclear if this would apply to the PSDs. This would only apply to the issue of debt securities from 1st July 2005 and would not apply to "*shares issued in substitution for shares of the same class already issued if the issuing of new shares does not involve any increase in the capital*".

The FSA has also confirmed that the London Stock Exchange created the ORB market in February 2009. The purpose of the market is to try and promote retail bonds to retail investors and to establish a liquid market in bonds admitted to the ORB. The ORB is a trading platform established by the London Stock Exchange to enable retail investors to trade bonds admitted to the ORB. The establishment of the ORB does not alter the view of the FSA, for securities to be traded on, the issuers still have to produce prospectus and ensure that they comply with the terms and conditions of the bonds. If an issuer breaches a requirement then the FSA can take action against the issuer, however if an issuer does not comply with the terms and conditions of the bonds (but is in compliance with the requirements of the FSA) then the FSA does not have the jurisdiction to intervene; bond holders are adequately protected under law and recourse to the issuer would be through the courts.

4.13 You also allege that the FSA authorised the release of a defective prospectus in 2007 (the 2007 Prospectus) which related to the change/substitution of the issuer, and also allowed Bank B to issue, what you describe as a coercive offer, to PSDs in June 2011. Whilst you clearly have concerns over the manner in which the prospectus was produced, I feel that it may be useful if I set out the FSA's role in the authorisation of such a document.

4.14 The FSA, as the UKLA, is simply required to review a prospectus which submitted to it by the firm and its advisers. The FSA role in this regard is set out in paragraph 3.1.7 of the Prospectus Rules. These rules set out that, in accordance with section 87A(1) of the Act, the FSA may not approve a prospectus unless it is satisfied that:

(a) the United Kingdom is the home State in relation to the issuer of the transferable securities to which it relates

(b) the prospectus contains the necessary information

(c) all of the other requirements imposed by or in accordance with this Part or the prospectus directive have been complied with (so far as those requirements apply to a prospectus for the transferable securities in question).

4.15 From this, it is clear that the FSA, as the UKLA, is not required by the Act to review each and every comment and statement which a firm makes within the prospectus. It also means that, providing the FSA is satisfied that the points set out under sections 87A(1)(a), (b) and (c) as set out on 4.12 above are addressed adequately the FSA is required to approve the prospectus and it is simply unable to vet or approve any information contained within the prospectus prior to the prospectus' publication.

4.16 In regard to the FSA's actions when approving the 2007 Prospectus, the FSA's role was as I have set out in paragraphs 4.12 and 4.13 above. Given the FSA's role, as set out by the Act and therefore *not by the FSA's own rules* (my emphasis) the FSA was simply required to ensure that the prospectus complied with the requirements of the listing rules (which incorporate any applicable EU Directives).

4.17 You are clearly unhappy with that situation. You appear to believe, perhaps erroneously, that the FSA had a statutory duty to consider the detail of the actual contents of the 2007 Prospectus and vet this *before* (my emphasis) it was issued. As I have explained above, the powers given to the FSA by Parliament under the Act simply do not allow to review (or vet) the contents of the 2007 Prospectus and in doing so consider what the proposed changes would mean for bondholders. Should the FSA have done this it would have acted outside of the powers given to it by Parliament and the courts could have overruled any actions or recommendations the FSA requested Bank B or Firm A to undertake to allow the approval of the Prospectus.

4.18 I would add that, although you are unhappy with the contents of the 2007 Prospectus and feel that the FSA should have not allowed publication in the format it did, you have not provided sufficient evidence to indicate that the FSA failed to fulfil its statutory requirements as set out and imposed upon it by section 87A(1) of the Act.

4.19 I have noted your comments regarding leading counsel's views on the prospectus and his view that the prospectus was defective. As I have explained, the FSA is required simply to ensure that the appropriate information is contained within the prospectus and not to check the accuracy of the information. The Act stipulates under section 87A:

(2) The necessary information is the information necessary to enable investors to make an informed assessment of—

(a) the assets and liabilities, financial position, profits and losses, and prospects of the issuer of the transferable securities and of any guarantor; and

(b) the rights attaching to the transferable securities.

(3) The necessary information must be presented in a form which is comprehensible and easy to analyse.

(4) The necessary information must be prepared having regard to the particular nature of the transferable securities and their issuer.

Having reviewed the information you have provided to both the FSA and my office it appears that Counsel's opinion (of why he believes the 2007 Prospectus was defective) appears to relate to the manner in which the information was portrayed rather than the fact that the information was not provided. Counsel, when providing you with his comments stated on page 6 of his opinion and says this:

Q4: WAS THE PROSPECTUS DEFECTIVE?

20. Yes.

(1) By reason of s. 87A of FSMA, the Prospectus was required to contain the information necessary to enable investors to make an informed assessment of (a) the assets and liabilities, financial position, profits and losses, and prospects of BOI and (b) the rights attaching to the Bonds.

(2) The Prospectus failed to provide the information necessary to enable investors to make an informed assessment of the rights attaching to the Bonds by:

(i) giving a misleading impression of the effect of the Scheme by (i) describing the substituted issuer as 'the UK branch of the BOI' when it was in fact BOI and (ii) wrongly stating that the effect of the Scheme was to transfer ***all*** of the obligations of B&W when (as explained) it did not transfer B&W's liability to be wound-up in England;

(ii) wrongly implying, by the description of the Bonds, that the Trustee had the right to commence winding-up proceedingsagainst BOI in England to enforce payment of principal and interest under the Bonds, when any such right was in fact unenforceable by reason of reg. 3(1) of CIRWR;

(iii) failing to explain in a form which was comprehensible and easy to analyse that the Trustee's only remedy to enforce payment of principal and interest under the Bonds was to commence winding-up proceedings against BOI in Ireland, and not England;

(iv) wrongly stating that the terms of the Bonds were based on English law when they were governed in material respects by Irish law, namely in relation to the winding-up of the Issuer (p. 13);

(v) failing to mention changes in Irish law as a risk factor relating to the Bonds (pp. 6 and 13);

(vi) misdescribing the authorised status of BOI (p. 8);

(3) The Prospectus contained a summary which was misleading, inaccurate and inconsistent when read together with the other parts of the Prospectus. Note in particular the contrast between:

(i) p. 7 (Subordination) and p. 13 (Risks related to subordinated Bonds); and

(ii) p. 7(Events of Default) and p. 21 (Events of Default).

4.20 The FSA, as the UKLA, may not approve (the prospectus) unless it was satisfied as to those aspects set out in Section 87A. You have not shown that the FSA has failed to fulfil its statutory duties in that respect. The FSA gave its reasons for taking the view that it took in its Stage One decision letter of 30th May 2012. I accept the validity of those reasons unless you are able to provide further and more detailed argument specifically why those reasons are not valid. In addition I should add that the same issue has been traversed a number of times in correspondence with the FSA. Merely stating now in your letter of 29th August 2012 that the FSA's response to the allegation (of the 2007 Prospectus being defective) is "*inadequate and incomprehensible*" is not a reason for me to take the view that the FSA's reasons are inadequate as set out in its Stage One decision or consequently that the FSA should not have approved the prospectus having regard to the provisions of Section 87A of the Act.

4.21 In response to my Preliminary Decision you have challenged the findings I set out above and maintain the "*supplementary prospectus is 'inadequate and incomprehensible'. This assertion refers to the FSA's position on taking no action to force the issuer to correct the misleading prospectus which is still the document on which potential purchasers of the Bonds must rely. I was specifically referring to Page 5, Point (iv) of the FSA's letter of 30 May 2012 which stated:*

> *'We sympathise with your assertion that the prospectus wrongly states that the terms of the PSD Bonds were "... based on English Law when they were governed in material respects by Irish Law ... ". But it could be argued that "based on English Law" is correct as it is the antecedent to the Bonds.'*

The prospectus is misleading on this point and bondholders went to considerable expense to have this confirmed by leading counsel. The FSA's response that including a historical but no longer correct key term in a prospectus does not require correction is what I consider inadequate and incomprehensible".

I appreciate that you feel that the:

> "*2007 Prospectus is the current prospectus lodged with the FSA/UKLA and available from the issuer's website and the one on which prospective purchasers and holders of the Bonds must rely for information. The Bonds are listed on the London Stock Exchange and subject to the Listing Rules which require an issuer to correct material inaccuracies in a prospectus. The FSA has the power under its rules to act and I would contend that it is an act of bad faith and neglect of duty for it not to do so*".

Although I can appreciate your views, I am not persuaded by them, Under FSMA 87G a supplementary prospectus can only be produced if a significant new factor, material mistake or inaccuracy occurs in the "relevant period". A relevant period is defined in 87G (3) as the period which begins when the prospectus is approved and ends with the closure of the offer of the transferable securities, or when trading in those securities on the regulated market begins.

In this case, the Bank B prospectus was approved in September 2007 and the bonds were admitted to the regulated market in October 2007. As the issuer is no longer offering the bonds as they are available from the regulated market, there is no requirement for the issuer to keep the prospectus up to date. Bank B prospectus is a document of public record and can be obtained by anyone for information purposes, and the document would no longer be used by a reasonable investor to make an investment decision as the prospectus relates to an 'offer' which was made in 2007 (which has therefore closed and as such given the events which have subsequently transpired is clearly out of date).

4.22 I would also add this. I have noted your concerns regarding the manner in which the FSA allowed Firm A to issue information to bondholders and your comments that this made it difficult for bondholders to consider the offer and, if necessary, obtain advice. Whilst the Listing Rules require bond holders to be provided with information, as bondholders they have a contractual relationship with the issuer (Firm A) concerning the time periods and how information will be distributed. That is set out in the terms and conditions. If an issuer has failed to adhere to these requirements then this is a contractual issue between the bond holder and the issuer and not one in which the FSA itself can become involved. I would however also add that the prospectus approved by the UKLA was produced to admit Bank B bonds to the regulated markets, it was not a public offer prospectus as you have suggested.

4.23 I also appreciate that you feel that Bank B made it difficult for bondholders to consider the offer but under the Listing Rules, there is no time period that bondholders have to be given to consider an offer. If the issuer had shares rather than bonds, then offer would have been subject to the Takeover Code requirements which does specify a time period but this simply *does not apply* (my emphasis) to bonds.

4.24 I would also add that the PSDs are held on trust for the bondholders by a trust company. Whilst you say that the bondholders themselves were unable to obtain the appropriate advice, as I am sure you are aware, the trustees have a legal or fiduciary duty to ensure that the bondholders' interests are protected. This is particularly relevant given Counsel's opinion on the enforceability of clauses regarding the winding up of the issuer as a result of default. I believe Counsel raised the trustees' actions with you. Given that my role is only to consider the manner in which the FSA has acted in this matter (and specifically the way in which it has considered your complaint) I have not enquired over the action of the trustees as this is clearly something which falls outside of my jurisdiction under the complaints scheme. For completeness I would add that although this falls outside of my jurisdiction it is unclear from your correspondence whether you have enquired about the trustees actions in this regard.

4.25 I appreciate that you say that you are aware "*that individual bondholders have tried enquiring of the trustee but have received somewhat threatening letters in return from the trustee's solicitors*". Whilst it is unfortunate that the trustees' solicitors have taken what I understand to be a defensive position, this does not mean that the FSA can become involved.

The FSA's role, as defined by the Act, is to regulate the financial services industry within the UK. Whilst I accept that the trustees are acting in relation to a financial product (i.e. PSDs) the trustees are not, in this instance, conducting a regulated activity and as such their conduct falls outside of the FSA's jurisdiction (both in a moral and legal capacity). As such if, as you appear to be suggesting in your correspondence with my office, you believe that the trustees have failed in their fiduciary duty, then this is a matter for the beneficiaries (for whom, the trustees act) to raise with them and, if appropriate, for the beneficiaries to refer to the courts. Unfortunately, this is not, no matter how sympathetic either I or the FSA may be, something we can assist you with.

4.26 On a similar basis, you have commented that the law governing the bonds has been changed from English Law to Irish Law. Although you have commented that the FSA allowed this, I believe that the FSA has previously commented to you that given that Ireland is a state within the EEA which has an established and trusted legal system it would have been difficult, if not impossible, for the FSA to provide a justifiable argument to the Court to prevent this change. This is a view with which I concur.

4.27 As I have set out above, the PSDs are held by a trustee on trust for the actual bondholders. The role of the trustee is a fiduciary one and as such it is required to safeguard the interest of those for whom it acts (namely the bondholders). I also believe that, under the trustee's powers it is able to change the governing law without the bondholders' agreement providing that it is satisfied that any changes to the governing law will not adversely affect the bondholders' interests.

4.28 Whilst you have alleged that the FSA has failed in its statutory duties, I note that you have not commented whether, despite the comments you received from Counsel, you have pursued a similar complaint against the trustees. This is particularly relevant as the trustee's have fiduciary duty which dictates that it *must* (my emphasis) act in the interests of the bondholders.

4.29 I would also add that the FSA has explained that the 2011 Exchange Offer was one made by Bank B, as the new issuer of the PSD, as part of a recapitalisation exercise that it had been required to undertake upon the instruction of the Irish Authorities. Given the manner in which this recapitalisation exercise had been undertaken, it was, I understand, not necessary for a prospectus to be produced. However, if one was, I believe that as the issuer of the PSD is now Bank B, responsibility for authorisation of the prospectus would have rested with the Irish Authorities *rather* (my emphasis) than the FSA.

4.30 Whilst you are unhappy that the FSA allowed Bank B to commence the Exchange Offer (which it is accepted that it did not complete), Bank B is, as you have set out on a number of occasions in your complaint, established and regulated in Ireland and operates in the UK on a banking licence. Given that Bank B, rather than the Firm A, is now the issuer of the PSDs, the FSA is simply unable to intervene directly in a recapitalisation exercise ordered by the Irish Authorities.

4.31 I have noted that you have stated in your correspondence that you believe the FSA should "*find a shred of humanity and use [its] considerable power and influence to intervene*". If the FSA had acted in the manner in which you had requested it would have clearly exceeded its authority and been acting *ultra vires*.

4.32 As I have set out above, given that Bank B was the issuer and bondholders have a contractual arrangement with Bank B (as it had replaced Society A/Firm A as original issuer), any dispute over a potential breach of contract is one which should be raised with Bank B. Any change to the level of payment bondholders receive does not fall within the FSA's jurisdiction as the bonds are not being brought to the market. Ultimately, the level of payment available for the PSDs is a contractual matter between the bondholders and the issuer.

5. My Final Decision

5.1 In brief I am satisfied that, the FSA has acted in accordance with its powers and statutory duties throughout in relation to this matter.

5.2 Whilst I can appreciate why you feel that additional legislation is needed, as I have set out above, complaints about the FSA's legislative function, whether concerning rules which are in place or are felt should be in place, are not things issues which can be considered under the rules of the complaints scheme.

5.3 It is unfortunate that the 2007 Prospectus is viewed as being defective. Whilst there are some aspects that some consider may be the case, there is nothing to indicate, given the FSA's role, that it failed to satisfy itself as to the 2007 Prospectus before approving it. I would add that, although you feel that the 2007 Prospectus is still in place the FSA has a different view to the effect that the 2007 Prospectus does not relate to the current transfer of the PSD but simply relates to the change of issuer.

5.4 When considering this, I have to be mindful of the fact that the 2007 Prospectus is entitled:

"*SUBSTITUTION OF*

The Governor and Company of Bank B

(acting through its United Kingdom Branch)

in place of

FIRM A"

Together with the fact that its description states:

"*This Prospectus is in relation to the substitution of the Governor and Company of Bank B (acting through United Kingdom branch)..., in place of Firm A ... as issuer in respect of GBP 75,000,000 13 3/8 per cent Unsecured Perpetual Subordinated Debt Bonds...*"

5.5 Given this explanation, in my opinion, I must concur with the FSA's view that the 2007 Prospectus relates *only* (my opinion) to the substitution of issuer and not to the issue of the bonds generally. Regardless of this, I am happy from the evidence presented to me that the FSA complied with its requirements under the Act when approving the 2007 Prospectus.

5.6 I sympathise with the position some bondholder find themselves in having lost out financially as a result of their decision to sell their PSD holdings in light of the Exchange Offer Bank B made. Whilst this is unfortunate however, it must be appreciated that following the Court's decision and approval in 2007, the issuer of the PSDs became the Irish regulated Bank B. Given that it was Bank B as an organisation and *not* (my emphasis) its entities which operate in the UK which made the decision to instigate the Exchange Offer, the FSA was unable to intervene in what is in reality and remains a dispute between a company and its creditors.

5.7 I appreciate that many of the PSD holders are elderly and originally invested in PIBS with Society A. This is not relevant however when considering the matter as a whole. Society A's *members* (my emphasis) voted to become part of Bank B in 1997 and, in doing so, became subject to corporate decision which were made by an overseas company and regulatory decisions made by an overseas regulator. It is unfortunate that this change of 'owner' also affected the holders of the PIBS when there was an exchange of those PIBS for PSDs.

5.8 Given the business decisions Bank B's management made, Bank B was required by its regulator to undertake a recapitalisation exercise. Further it has to be recognised that as the issuer of the PSDs was Bank B, the Exchange Offer is a matter for Bank B, its Irish Regulator and the holders of PSDs. It is unfortunate, but the FSA simply is not involved in the decision relating to how Bank B is capitalised (of which the PSDs form part).

5.9 I appreciate that you maintain your belief that the "*Exchange Offer was clearly in breach of [Disclosure Rules and Transparency Rule] DTR 6.1.3(2) but the FSA took no action to rectify this even when it was brought to their attention. I contend that this was an act of bad faith on the part of the FSA.*

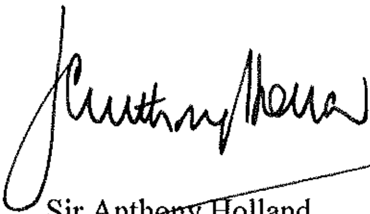
Furthermore if rules such as DTR 6.1.3(2) cannot be used to ensure equal treatment of bondholders who are entitled to the same them the FSA should have taken steps to explain why this is not the case so that investors do not wrongly feel they are afforded FSA protection against unfair acts by bond issuers".

5.10 Whilst you may hold this view ultimately Bank B is an Irish incorporated entity, even when acting through its London Branch; the London Branch is not a separate legal entity. The Prospectus Directive provides issuers of debt securities with denomination of greater than €1,000 to choose its home member state Article 2(M)(2) Prospectus Directive. The election of UKLA as the Home Member State under the prospectus directive is only in relation to the individual issuance of debt securities. (which in this case relates to the 13 3/8 per cent PSDs). Importantly it does not mean that the FSA is then the home regulator for other regulatory requirements that may be applicable to Bank B. Bank B as an Irish incorporated bank will be subject to the regulation of the Central Bank of Ireland and not the FSA.

5.11 DTR 6.1 sets out the information requirements applicable to issuers of shares and debt securities. The purpose of this chapter is to ensure that securities holders receive the same information so that they are able to exercise their rights. DTR6.1.3(2) requires an issuer of debt securities to ensure that all holders of debt securities ranking *pari passu* are given equal treatment in respect of all rights attaching to those securities. This paragraph however has to be read within the subject of the chapter which is the provision of information. DTR 6.1.3(2) is requiring an issuer to ensure that the same information is provided at the same time to all bond holders that rank equally so that they can then exercise their rights in an informed position.

5.12 Given that all those which chose to accept Bank B's offer would have been able to do, with the all transaction taking place at the same date (and without preference being given to any party) it would appear to me that Bank B complied with this requirement. Although I accept that many of the bondholders were unable to accept the offer within the set time scale, this appears to have been the direct result of the manner in which the *bondholders chose* (my emphasis) to hold their bonds rather than as a direct result of the criteria imposed by Bank B. As such, this indicates to me that Bank B complied with the relevant requirements of the DTR to which you have previously referred.

5.13 My Final Decision is therefore that your complaint should not be upheld for the reasons that I have set out above.



Sir Anthony Holland
Complaints Commissioner

5th March 2013