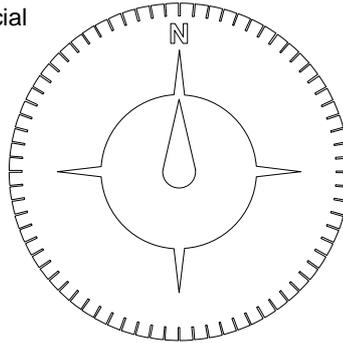


## Financial Advisers: One Step Forward, Two Steps Back?



A round up of recent  
developments affecting Financial  
Advisers and their Insurers

Go further



**Harriet Quiney**  
**Partner**  
27 February 2013

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## Summary



Arch Cru Consumer Redress Scheme and its implications for mis-selling cases

Clark & Clark v In Focus Asset Management & Tax Solutions Ltd – do IFAs now face double jeopardy?

FSCS v Various IFAs (Keydata) - lessons to be learned from a compensation scheme on the war path

Appointed representatives – what can you do if they go AWOL?



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## Consumer Redress – lessons to be learned

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## Arch Cru Consumer Redress Scheme

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- Two Open Ended Investment Companies (“OEICs”) with the ability to invest in a wide range of asset classes
- Both funds were Non-UCITS Retail Schemes (“NURS”)
- Invested in Guernsey incorporated cell companies
- Operated by Capita Financial Managers Ltd (the Authorised Corporate Director)
- BNY Mellon Trust & Depositary Ltd and HSBC Bank plc were depositaries
- CFM delegated the role of investment manager to Arch Financial Products LLP
- Cru Investment Management Ltd distributed and marketed the funds to IFAs

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## Arch Cru Consumer Redress Scheme

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- Funds suspended 13 March 2009
  - Because they were illiquid
  - Could not generally redeem, purchase or transfer shares
- NAV supposed to be £362.7m
  - Following sales of various assets valued at £96.3m remainder said to be £83m
  - Shortfall of £183.4m
- 21 June 2011 Capita, Mellon and HSBC announced a payment scheme worth £54m
  - Shortfall £129.4m (now estimated at £140.5m)



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## Arch Cru Consumer Redress Scheme

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- FSA consultation paper April 2012
  - s404 scheme
  - Compulsory
  - £110m redress to between 15,000 and 20,000 consumers
  - Cost £6m - £11m
- 230 responses: “...the majority of respondents were opposed to our proposals”.
- FSA policy statement December 2012
  - s404 scheme
  - Opt-in
  - £20m- £40m redress to between 3,000 and 6,000 consumers
  - Cost £0.6m - £2.7m



## Arch Cru Consumer Redress Scheme



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We are not applying hindsight or expecting IFAs to spot potential mismanagement – we expect IFAs to have made an assessment of the risk of the types of assets that the fund managers stated the funds would be invested in, not what they actually invested in if it was different.

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A reasonable competent IFA ...should have concluded that these funds were high risk investments and therefore only recommended them to consumers who were willing and able to take this level of risk

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We grouped consumers ...into three broad categories based on the type of investment they would have made if they had received suitable advice:

- Consumers who should not have been advised to take any capital risk with their investment;
- Consumers who could have been suitably advised to take a small amount of risk with their capital
- Consumers who, if suitably advised, could have taken some risk with their capital

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The consumer's capacity for loss ...is different to the level of risk that the consumer was willing or would have preferred to take. ...consider whether:

- The consumer was able to take any risk with the consumer's capital or interest;
- There would have been an impact on the consumer of a total or partial loss of capital;
- The consumer could, considering his personal and financial circumstances, afford to take this level of risk.

## Arch Cru Consumer Redress Scheme



- Scheme to come into effect in April 2013
- Consumers to opt in by July 2013
- Review outcomes by December 2013
- Payments within 28 days of review
- 100 firms may fail (about 15%-20%)but 110 have already cancelled their permissions

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## Double jeopardy – to sue or not to sue

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## To sue or not to sue – Clark & Andrews

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- s228(5) FSMA: *“If the complainant notifies the ombudsman that he accepts the determination, it is binding on the respondent and the complainant and final”.*
- FOS limit £150,000 but it can “recommend” that firms pay a larger amount
- Can the complainant accept the award and then sue for the balance?
- Andrews v SBJ Benefit Consultants Ltd [2010] EWHC 3669 (QB)
  - Doctrine of merger
  - A person who has obtained a judgment in a tribunal with appropriate powers and jurisdiction cannot later recover in court in respect of the same matter
- Clark & Clark v In Focus Asset Management & Tax Solutions [2012] EWHC 2875 (Ch)
  - FOS is not a tribunal and determines complaints not causes of action

## To sue or not to sue – Clark & Andrews



- Likely that the matter will be decided on appeal
  - FOS is not a tribunal is “difficult”
  - R (Heather Moor & Edgecomb) v FOS [2008] EWCA Civ 642 proceeded on the basis that FOS was a tribunal for the purposes of Article 6 ECHR
  - Clarks more “sympathetic than Andrews”



## To sue or not to sue – Clark & Andrews



- While we wait for the appeal:
  - Post Andrews firms were asked if they would pay a recommendation so the consumer could decide how to proceed
  - Extension of time limit for acceptance with agreement of all parties?
- April 2012 Mark Field MP tabled an amendment to the FSMA which would allow consumers to accept award and sue of Legal Services Act 2007

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## A compensation scheme on the warpath

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## A compensation scheme on the warpath

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“ FSCS is funded by the industry, and we must be able to demonstrate that we provide value for money. This covers both the efficiency with which we provide our services and our effectiveness in making recoveries from the estates of failed businesses or other parties where applicable. ”

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## A compensation scheme on the warpath

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- FSCS: Compensation fund for customers of failed financial services firms
- The Scheme actively pursues opportunities to recover the costs of compensation
- A key focus of FSCS's efforts is the estates of the banks which failed in 2008
- FSCS v Various IFAs (Keydata)
- FSCS allegedly keen to apply commercial analysis to its approach to recoveries
- Third Party (Rights Against Insurers) Act 1930



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## A compensation scheme on the warpath

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- FSCS v Various IFAs (Keydata)
  - Keydata (the provider) was placed into administration in June 2009
  - Compensation (up to £48,000) paid to customers in return for assignment of rights
  - FSCS is pursuing the financial advisers who sold the products
  - Proceedings issued by the FSCS against advisers from November 2011
  - £3.9m budget 2012/13, £7.7m 2013/14 and £7.2m 2014/15 (proposed)
  - Total recoveries expected to be £75m (£30m from Norwich & Peterborough)



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## Appointed Representatives

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## Appointed Representatives

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- s39 FSMA

- (1) If a person ...is someone for whose activities in carrying on the whole or part of that business his principal has accepted responsibility in writing, he is exempt from the general prohibition in relation to any regulated activity comprised in the carrying on of that business for which his principal has accepted responsibility.
- (3) The principal of an appointed representative is responsible, to the same extent as if he had expressly permitted it, for anything done or omitted by the representative in carrying on the business for which he has accepted responsibility.



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## Appointed Representatives

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- What happens if a AR goes AWOL?
  - Sells a product the principal knows nothing about?
  - Sells a fraudulent product the principal knows nothing about?
  - Can the consumer go to FOS?
- Complainant must (in effect) be a “customer” of the respondent
- Must FOS apply UK law?
  - Generally FOS only needs to have regard to the law
  - Yes when it comes to jurisdiction
  - Emmanuel v DBS Management plc [1999] 2 Lloyd's Rep PN 593 (s44 FSA 1986)



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## Conclusions

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## Conclusions

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- IFAs are an unusual PI risk class
- In some ways more like a cat risk
- The FSA, FSCS and FOS have been something of a game changer
- Some insurers have come in and left quickly
- We have recently seen a number of established names leaving
- Unlike the last crisis one cannot just rewrite the minimum terms
- Will be anyone left?



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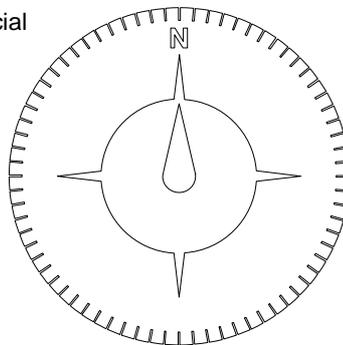
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