

On 31 January 2005 the Complaints Commissioner issued a final report on complaint GE-L0332 to the complainant and the Financial Services Authority. The introduction and summary to that report is published below.

CONFIDENTIAL

FINAL REPORT AND FINDINGS

1. Summary

1.1 This is the report of an investigation by the Complaints Commissioner of complaint reference number GE-L0332 against the Financial Services Authority (FSA). The complaint falls to be considered under the Main Complaints Scheme.

1.2 The complainant is an individual who, on 27 September 2002, had purchased 11,850 shares in an Open-Ended Investment Company [OEIC], X Ltd, via an intermediary, for £6,000. Part of the promotion of the investment was that the income would be paid quarterly: the first payment being at the end of April 2003.

1.3 In January 2003 he received notification from X Ltd that the income payments, instead of being paid quarterly, would be paid on a monthly basis commencing in April 2003 due, it said, to overwhelming demand from their clients and their financial advisers to do so. He received the first monthly payment at the end of April 2003.

1.4 The complainant advised X Ltd that he did not agree to the change but the company rejected his complaint and referred him to the Financial Ombudsman Service [FOS]. He made his formal complaint to the FOS on 7 April 2003 and this was rejected by letter dated 22 August 2003 on the grounds that X Ltd, under Section 21 of the Open-Ended Investment Company Regulations 2001, had correctly submitted a written proposal to the FSA on 9 December 2002 to alter the timing of the payment of income and, as no objection had been received from the regulator, the change had been implemented on 10 January 2003 and all investors notified accordingly. The complainant then took his complaint to the FSA by letter of 3 September 2003. The FSA Consumer Contact Centre [CCC] handled the correspondence and explained the process that the company had gone through to allow the change on the timing of income payments to take place.

1.5 The complainant did not find this satisfactory and wrote to the Complaints Commissioner on 15 December 2003. This letter was acknowledged and a substantive reply was sent on 4 February 2004 which explained that, as it was a complaint against the FSA, the Commissioner would normally allow the FSA to investigate and respond first before the Commissioner became involved. A letter was also sent to the FSA Company Secretariat, which is the department that administers the formal Complaint Scheme, requesting that the complaint be investigated. The substantive response to the FSA's Stage 1 investigation was sent to the complainant on

2 June 2004 together with an apology for the delay in replying. The complaint was not upheld.

1.6 The complainant wrote again to the Commissioner by letter of 19 June 2004 stating that he was dissatisfied with the FSA's findings and asked that the matter be investigated further. The FSA's file was received from the Company Secretariat in August 2004 and the Commissioner wrote to the complainant on 8 September 2004 stating that he would undertake a Stage 2 investigation.

1.7. In the course of the investigation, the Commissioner has obtained and has considered written representations from the complainant and documents and correspondence provided to him by the complainant and by the FSA. Interviews have been held with members of the FSA staff. No information was withheld by the FSA for confidential reasons.

1.8. The Commissioner has analysed the complaint as having two components -

First, the substantive complaint being that the FSA did not exercise *due care* when allowing/agreeing that X Ltd could change their timing for payment of income on an OEIC, in which the complainant had invested, from quarterly to monthly payments from April 2003 thereby allegedly causing the complainant financial loss; and

Second, that the complainant was dissatisfied with how the FSA handled his complaint, originally by the CCC and then by the Company Secretariat when the complaint had been entered into the formal Complaints Scheme.

2. Findings

2.1 In respect of the substantive complaint, the Commissioner has considered the following -

(a) The complainant relies on the fact that the investment was promoted as giving an income payable quarterly. He challenges the statement made by X Ltd that it was due to overwhelming requests from investors and their financial advisers that X Ltd chose to change the payments to monthly. He argues that by doing so, the fund would suffer higher administration charges and on a small investment such as his he would be financially disadvantaged. His view is that there are many other funds available that offer monthly payments for investors and that it was because this fund offered quarterly payments he chose to purchase his shares and thereby he had a contract with X Ltd to make the income payments quarterly. He alleges that the FSA were not party to that contract and, therefore, by allowing X Ltd to change the timing of the income payments did not exercise *due care*.

(b) The power to permit changes to unit trust schemes is contained in the Financial Services and Markets Act 2000 but changes for OEICs would come under the jurisdiction of a Statutory Instrument [SI]: the Open-Ended Investment Companies Regulation 2001. Under Regulation 21(1)(b) of that SI written notice must be given for any proposed alteration to the OEIC's prospectus which, if made, would be significant. By Regulation 21(3) effect could not be given to any such

proposal within Regulation 21(1) unless the FSA had given its approval in writing; or at the expiry of one month, (beginning with the date on which notice of the proposal was given), without the OEIC (or the depositary) having received from the FSA a warning notice under Regulation 22.

(c) Solicitors for X Ltd notified the FSA by letter dated 9 December 2002 of four changes that X Ltd wished to make to this particular OIEC one of which was subsequently withdrawn. This was received on 10 December 2002. One of these requests constituted giving notice of the change on income payments from quarterly to monthly for the sub fund in which the complainant had placed his investment. In the response from the FSA of 24 December 2002 to the solicitors for X Ltd the other two requests seeking to introduce further sub funds were formally approved but no comment was made on the change of timescale of income payments for the sub fund in which the complainant had invested. Although the FSA did not explicitly comment on the timing of this change, X Ltd was entitled to deem that this was approved from 8 January 2003 in line with Regulation 21(3) of the SI (see paragraph (b) above). The solicitors confirmed by letter dated 16 January 2003 to the FSA that the two approved sub funds had been created and that the change made to the timing of income payments on the complainant's sub fund implemented. Whilst not required to do so by the FSA, X Ltd did give three months written notice to those investors affected in respect of that sub-fund.

(d) By the wording of Regulation 21(1)(b) of the SI an OEIC could make changes to its prospectus if they were not *significant* changes without consulting the FSA. The Commissioner understands that the solicitors to X Ltd may have considered the changes to the timescale of income payments *significant* by mentioning them in their letter of 9 December 2002 or they may have included them for completeness. The FSA have indicated that they are aware that such changes in reducing the timescale for payment of income have been made in a prospectus where the solicitors acting for the OEIC in question had chosen not to notify the FSA as they had presumably deemed that the change was not *significant*.

(e) The FSA have stated that it is extremely unusual for no comment to be made about a particular request for change to a prospectus in that in the vast majority of cases each change was normally acknowledged and commented on. In this case, being the timing of the distribution of income moving from quarterly to monthly, the FSA state that they would have no basis to raise objection to the change since, in their view, there was no obvious disadvantage to investors receiving income distributions more frequently and, should an investor not wish to remain in a monthly income distribution fund, they would be given time to move their investment either to another fund within the "group" or outside to another provider. It was a matter of a commercial decision between X Ltd and its clients. However, in the FSA's view, if the request for income distributions for a particular fund was that it should be paid half-yearly, or yearly instead of monthly, then the FSA would want to ensure that the rationale was clearly disclosed to investors as it might be important to an investor to

have a steady regular income rather than a lump sum twice or once a year.

(f) On the request of the Office of the Commissioner, X Ltd has provided information to the FSA on the additional cost of making monthly instead of quarterly income payments in 2003 in respect of the sub fund that the complainant had invested in. The effect of moving to a monthly rather than a quarterly basis was to increase costs charged to the fund from approximately £15,000 to £44,000 per year. In proportionate terms, the increase represented approximately 0.03% of the fund value in 2003. At its current size, the cost difference is closer to 0.01%. In respect of the investment of £6,000 by the complainant the extra cost associated with his investment would have been approximately £1.80 (one pound eighty pence) per year. He would have, however, benefited from the accelerated payments because he would have been able to invest that income paid monthly elsewhere if he so wished.

(g) X Ltd has confirmed that whilst they do not have formal research on file to document that the change was in response to client demand, they do confirm that the change was prompted by the feedback from major brokers that the lack of a monthly distribution was a major barrier with clients to invest as monthly distributions had become an almost standard feature of this type of high income fund.

(h) In summary, X Ltd complied with the regulations in seeking to make a change to the timescale of its income payments on this particular sub fund. It also, whilst not required to do so, gave three months written notice to those investors affected. The request, whilst not to the complainant's liking, was as a result of feedback from its marketing forces and hence a commercial decision. The FSA has taken a not unreasonable view that they would not normally object to increasing the number of income payments of an OEIC. In practical terms, the complainant has had a reduction in his payments due to increased administrative costs of £1.80 per year but this possibly could be offset by the fact that an earlier payment would have allowed him to reinvest some or all of his monthly income or, alternatively, he had the opportunity to withdraw his funds and reinvest elsewhere. On the evidence before him, the Commissioner does not uphold this component of the complaint.

2.2 On the second component of the complaint, the Commissioner has considered the following –

(a) The complainant wrote to the FSA on 3 September 2003 to make his complaint against X Ltd and asked for details of the legal authority under which the FSA were able to vary a contract between him and X Ltd. As he did not receive a reply he wrote again on 24 September 2003 asking that the information requested was sent to him for immediate use. The CCC responded on 1 October 2003 apologising for the delay in replying and stated that the request had been received in December 2002 from X Ltd seeking approval for various changes, which were granted in December 2002. They stated

"The request was submitted to the FSA as required under regulation 21 of the Open-Ended Investment Companies Regulation 2001. These regulations govern how proposed alterations to schemes such as (name of X Ltd) scheme must be approved by us."

(b) The complainant replied by letter of 4 October 2003. He queried the fact that the FSA letter was not signed by an individual and stated that his earlier points had not been dealt with in that the investment had been promoted on the basis of paying income quarterly and the FSA should not have agreed to the change, thereby ignoring the terms of the promotion. He stated –

"...Consequently as this investment was promoted on the basis of paying income quarterly you should not have agreed to the change, and the fact that such a request was received by you surely does not mean that you have to agree to it, ignoring the terms of the promotion."

The complainant sought compensation. The CCC replied on 22 October 2003 recognising that the complainant remained unhappy but repeated their earlier comments on how the regulation had been approved under regulation 21 of the Open-Ended Investment Companies Regulation 2001. They explained that the letter was unsigned because the CCC team sent out the correspondence and it was not dealt with by an individual contact. The letter was addressed incorrectly. The complainant replied by letter 31 October 2003 referring to the incorrect addressing of the correspondence and stating

"I can assure you that I am much more than just unhappy by your action. I am also not satisfied with your response, and accordingly will pursue my complaint."

(c) The complainant then wrote to the Office of the Commissioner on 15 December 2003 and the correspondence was acknowledged and forwarded to the FSA Company Secretariat as it was analysed that the complaint was against the FSA itself. The FSA received this correspondence on 5 February 2004, acknowledged receipt on 12 February 2004 and confirmed by letter of 19 February 2004 from Officer A that the matters raised would be investigated under the formal Complaints Scheme. That letter confirmed that the complaint had been entered into the Scheme with effect from 5 February 2004.

(d) Officer A sent a holding letter on 4 March 2004 and again on 1 April 2004, the latter indicating that the review of the complaint was subject to a final analysis and that the complainant should be provided with the conclusions shortly. The substantive reply was sent on 2 June 2004 and did not uphold the complaint. In that letter, the FSA also stated that the correspondence from the complainant to the CCC did not constitute a complaint under the formal Complaint Scheme until his letter of 15 December 2003 addressed to the Complaints Commissioner had been received by the FSA on 5 February 2004.

(e) The formal Complaints Scheme requires the FSA to acknowledge the correspondence within five working days of receipt of the complaint, if the investigation is not completed within four weeks

an explanation of a likely completion date should be given, and the investigation should be completed within eight weeks. In this case, the FSA did acknowledge the complaint within five working days and sent a holding letter four weeks later. However, their substantive response from Officer A, which included an apology for the delay, was not sent until some seventeen weeks later. A separate letter accompanied that response from Officer B for the Company Secretariat that stated -

"...I am writing to apologise for the unreasonable delay that has occurred in answering your complaint.

"Due to high volumes of work received by the Complaint Team, and other resourcing issues, I am afraid that a small number of complaints have taken far longer to complete than anticipated, which has meant that we have missed some of our strict service level standards. Unfortunately your complaint was included within this group and its progress and completion was delayed. We are continuing to address the issues giving rise to the delay, including those relating to the performance of our staff.

"..Again, please accept my sincere apologies for the delay in answering your complaint, and the fact that we did not meet our service level standards in your case."

(f) In summary, the complainant's initial contact at the FSA was with the CCC that did provide as requested, albeit belatedly, the details of the legal authority under which the FSA could approve a change to an OEIC. When the complainant again expressed his dissatisfaction by letter of 4 October 2003, the CCC repeated the information but acknowledged that this would not resolve his grievance. The CCC correspondence did contain an apology for the delay in responding to his enquiries. The FSA's view is that these letters from the complainant to the CCC did not constitute a complaint against the FSA as disputes over matters referring purely to the FSA's discretion, where this is not accompanied by an allegation of misconduct, did not qualify for inclusion in the formal Complaints Scheme. It is the Commissioner's view, however, that the dissatisfaction expressed in the complainant's letters, in particular those of 4 and 31 October 2003, and taken as a whole with his other correspondence, did constitute a potential complaint against the FSA and warranted a referral to the Company Secretariat for an overview. Following the involvement of the Secretariat, the FSA did not meet the standard of service as required by the Complaints Scheme. For these reasons the Commissioner, therefore, upholds this component of the complaint.

2.3 (a) The Commissioner is aware that the CCC has improved its service standards in general since 2003 and correspondence is now signed individually under the manager's name as opposed to a general signature depicting the CCC. Also a "*Complaints Awareness Campaign*" was instigated by the FSA in July 2004 to assist all employees to recognise a potential complaint against the FSA.

(b) In respect of the Company Secretariat, he is aware that further resources, both financial and an increase of personnel, have been

provided to that Department during 2004 and a new "Fast Track" process incorporated into the formal Complaints Scheme launched on 1 October 2004 styled to handle complaints more quickly and efficiently. A complaint such as this does, however, highlight the need for vigilance by all departments of the FSA in analysing whether the expression of dissatisfaction by a consumer individual or firm should be included into the formal Complaints Scheme. However, the Commissioner is aware that this new scheme implemented from October 2004 will be monitored closely, and by letter of 2 June 2004 from Officer B a separate formal written apology has already been sent to the complainant. For these reasons the Commissioner does not make any specific recommendations following the findings in this complaint.

- 2.4 The Commissioner has decided to publish the above Summary and Findings.

January 2005