Before the Arbiter for Financial Services

Case No. 433/2016

GJ (“*the complainant*”)

vs

Hollingsworth International Financial Services Ltd. (C32457)

(“*the provider of financial services*” or “*service provider*” or “*provider*”)

Sitting of the 15 January 2019

Summary of the Complaint and the Provider’s Response

The Complaint

The complaint document was submitted to the OAFS on 15 September 2016. The last submissions made by the parties were filed on 9 July 2018.

The complainant, 83 years of age, is British and a resident of Malta since 1992. Her sources of income in 2011 were her pension and investment income.[1]

In April 2011, Paul Tilbrook (employed with the service provider) visited her home on her request and compiled a Fact Find. At that time, she held investments in equities and bonds which were managed by a London firm of stockbrokers. She also held funds on deposit in a number of offshore bank accounts. The complainant was fearful that her bank deposits in the Isle of Man and Channel Islands would not be sufficiently safe and asked the provider for something more secure.

[1] *A fol.* 52

The complaint document states that she "*vividly remembers*" informing the representative of the provider that her investment attitude was "*cautious or medium*".[2] The complainant was categorised by the provider as a Retail Client.[3]

The provider prepared a Personal Recommendation Report ("PRR") dated 20 April 2011.[4] The PRR is a five-page document in which the provider gives a brief overview of its services, outlines its recommendations and charges and describes how the investments will be allocated between different products. In its Recommendations,[5] the provider confirms that advice had been requested for a capital sum of GBP220,000 and USD108,000 held with Anglo Irish Bank. It refers to the protection of up to GBP85,000 for deposits per individual per bank and "*For this reason, it makes logical sense to move funds to a much more protected structure whilst still retaining your investments offshore status.*"[6]

The provider includes "*initial suggestions for investments*" and writes, "*I have deliberately included a range of capital protected structures and funds that will provide you with more diversified portfolio than you presently hold. As new opportunities arise, we will suggest these to you and recommend that they become part of your overall investment strategy. Our role is to monitor each fund in the portfolio and recommend changes accordingly. This 'active management' principle means that changes can be made quickly and cost effectively.*"

A total of GBP408,001 and USD58,831 were transferred to a new account with a custodian, Ned Bank Jersey office (formerly Fairbairn Private Bank Jersey Office), for investments to be affected through the services of the provider.[7] Between June 2011 and 2015, the complainant entered into *circa* 40 purchase transactions, all of which in index-linked financial instruments.[8]

Paul Tilbrook used to personally deliver investment recommendations - in the form of letters signed by the provider and addressed to the complainant - to her residence. A number of such letters of recommendation, diversely dated, were

[2] *A fol.* 54, Paragraph 2.3
[3] *A fol.* 120
[4] *A fol.* 121
[5] *A fol.* 123
[6] *Ibid.*
[7] *A fol.* 58, Paragraph 2.8
[8] *A fol.* 63, Paragraph 2.12

attached to the complaint. The complainant observed that at the end of each recommendation letter, the provider would end with the following declaration:

"*Please note that this/these structured notes is/are deemed a complex instrument and that I deem it to be suitable for your investment needs.*"[9]

According to the complainant, the investments recommended to her in these letters were intended for Professional Clients and Eligible Counterparties.[10]

The market value of her portfolio fluctuated over the course of this time. Up to September 2014, the value was around GBP400,000, but then it fell in value to around GBP241,329 in December 2015, which at this time consisted of 11 equity-linked complex index notes.[11] The complainant claims that the capital loss as at 31 December 2015 stood at GBP203,387 representing 48% of her capital invested.

The loss widened as at June 2016[12] and stood at GBP221,799 (50% of her investment). The loss was based on a portfolio of 10 equity-linked index investments, which had not yet matured or called up by the issuer.

According to the complainant, she never met the provider until December 2015.[13]

The complainant lists the following[14] as claims and remedies that she is requesting:

1. To declare that the Respondent Firm failed its obligations towards its client when it refused to provide copies of any Client Profile or Client Fact Find or Questionnaire it may have compiled on her person;
2. To declare that the complaint submitted against the Respondent Firm constitutes a case where the latter has not acted in the best interests of its client and has failed its fiduciary obligations towards its client;

[9] *A fol.* 61, Paragraph 2.10
[10] *A fol.* 62, Paragraph 2.11
[11] *A fol.* 63, Paragraph 3.1
[12] *A fol.* 64
[13] *A fol.* 59, Paragraph 2.9
[14] *A fol.* 97 *et seq.*

3. To declare that, as a result of the misconduct of Respondent Firm, the provider did not perform its obligations, including those of a contractual nature, towards the complainant when as a result of *culpa lata*, gross negligence and recklessness, it committed investment misselling;

4. To declare and order the Respondent Firm to compensate the complainant and reinstates her in her former financial position, namely the one antecedent to the capital invested on the advice of the provider, with interest and, simultaneously, transfer the legal and beneficial title of her portfolio held in custody with Nedbank, together with a subrogation in favour of the respondent firm for all residual rights in the same investment;

5. That in the event of a monetary value exceeds the amount competent to the Arbiter to award in terms of article 21(3)(a) of Cap. 555, the Arbiter shall recommend to the Respondent Firm to pay the complainant any balance in excess of such sum in terms of article 21(3)(b) of the same Act;

6. To declare and order the Respondent Firm to pay interest at a fair and reasonable rate for a period from 1 June 2011, and the date of effective restitution of the capital invested of GBP444,716.

7. Costs for the Respondent Firm.

The Reply of the Service Provider[15]

1. The service provider declares that the copious evidence submitted in the complaint is inadmissible and should be struck off by the Arbiter;

2. The complaint is null and inadmissible as it is not in 'summary form';

3. The Arbiter does not have the competence to hear the complaint on the basis that monetary compensation being demanded is in excess of EUR250,000;

[15] *A fol.* 362 *et seq.*

4. The Arbiter cannot consider the remedy being sought by the complainant in paragraph 4(iii) page 47 of the complaint owing to the fact that the Arbiter does not have the competence to order such remedy and in doing so would be acting '*ultra vires'* to his functions and powers of adjudication;

5. The complaint is time-barred by the lapse of five years since the contractual relationship between the company and complainant was concluded on 20 April 2011;

6. The company rejects the allegation in paragraph 2 and 3 of Section titled '*Claims and Remedies being requested by the Complainant*' which allegation refers to the conduct of the company as fiduciary obligations arise in virtue of law, contract or assumption of office or behaviour whenever a person (and not a financial services provider) exercises control in accordance with Article 1124A of Cap. 16 of the Laws of Malta;

7. The complaint is unfounded in fact and at law, and should be dismissed;

8. That any losses suffered by the complainant were exclusively as a result of factors inherent to the investment purchased by the complainant such as market risk, credit risk or fraud risk, and not as a result of omissions of the company or its agents or employees which always acted in the complainant's regard in accordance with applicable laws and rules;

9. As to the merits of the case, the provider's claims are summarised as follows:

   (a) The role of Paul Tilbrook: The company claims that Mr Tilbrook never gave investment advice. His role was simply collecting the necessary information by assisting the complainant with, among other things, the completion of the company's Confidential Client Fact Fund.[16]
   (b) The Key Information Documents (KIDs): The provider claims that the designations on the KIDs which were marked as "*For Professional Investors and Eligible Counterparties Only: not Suitable for Retail*

[16] *A fol.* 365, Paragraph 9(a)

Distribution" related to the marketing document (that is, the KID) and not the underlying product.[17]

(c) Relevance of the Products being Complex Products: The service provider claimed that it is untrue that complex products cannot in all circumstances be suitable for Retail Clients. The products which were offered to the complainant were actually lower risk than holding the actual equities (which the complainant is, by her own admissions, familiar) and, therefore, fit within her risk tolerance and investment objectives.[18]

(d) Provision of copies of Internal Documentation: The company claimed that there were no regulatory obligations to provide copies of internal documentation – such as the Confidential Client Fact Find or other documents – to the complainant.[19]

(e) The Timelines for Replies to the initial complaint: The service provider rejected that it breached the regulations and went beyond good industry practice when it delayed in providing a reply to the complainant within two months. It said that it was reasonable for its assessment to take time.[20]

(f) Documentary evidence relating to preceding investment experience: The provider stated that information that is required to be collected under this SLC could be collected orally and under SLC 2.24 was entitled to rely on the information provided by its client unless it is aware or ought to be aware that the information is out of date, inaccurate or in

(g) The Suitability Assessment: The provider claimed that the suitability was satisfied in relation to the complainant. It emphasized that the nature of investment advice is based on professional judgement and by its nature highly subjective.[21]

[17] *A fol.* 366, Paragraph 9(b)
[18] *A fol.* 366, Paragraph 9(c)
[19] *A fol.* 367, Paragraph 9(d)
[20] *A fol.* 368, Paragraph 9(e)
[21] *A fol.* 370, Paragraph 9(e)

10. That accordingly, and always without prejudice to the above, the Complaint is unfounded in fact and at law and should therefore be rejected with costs because:

(1) With regards to the First Remedy being sought by means of which the Complainant demands a declaration that the Respondent Firm failed its obligations towards its clients when it refused to provide copies of any client Profile or Client Fact Find or Questionnaire it may have contiled on her person as requested by Finco Treasury Management Ltd's letter to the Respondent Firm dated 2nd February 2016.

The company is not authorised to and does not hold and control clients' monies or assets (nominee services) or provide discretionary portfolio management services. Services offered to and provided to the complainant were limited to investment advice and, where the complainant agrees to accept the company's recommendations, reception and transmission of orders. In this case, the complainant agreed to use Nedbank as custodian and broker.

As the company provided neither of the services of acting as nominee or discretionary portfolio management, issuance of statements or valuations of holdings was not a regulatory or contractual requirement. This particularly since (as also confirmed in Complainant's letter) Nedbank provided such statements and valuations.

For the above reasons, the complainant's complaint is in our view unfounded. Complainant could have asked for valuations from the Company as an additional service but this was neither requested nor offered. We take this opportunity to refer complainant to Nedbank for the type of details, which she is requesting in relation to her bank accounts and investment portfolio, held with Nedbank.

(2) With regards to the Second Remedy requesting a declaration that the Complaint submitted by the Complaint constitutes a case where the latter has not acted in the best interest of its clients and has failed its fiduciary obligations towards her client including those emanating from Articles 1124A and 1124B of the Civil Code when these obligations "arise in virtue

of law, contract quasi-contract, trusts, assumptions of office or behaviour."

The complainant's claim is unfounded as the company has always acted in a professional manner and has always operated with a given level of competence and conducted business with the complainant in a manner that is of an adequate standard as is required by the financial services regulatory framework and as shall be amply proved by means of written testimonies as well as ample documentary evidence;

(3) With regards to the Third Remedy demanded a declaration that as a result of the misconduct of Respondent Firm, HIFS did not perform its obligations including those of a contractual nature, towards the complainant when as a result of culpa lata, gross negligence and recklessness, it committed investment misselling;

The complainant's demand is unfounded as it shall be amply proved to the Arbiter that first investment made by the complainant was suitable for her. All subsequent recommendations provided to the complainant were similar in complexity and in addition complainant had over the years of investing accumulated significant additional experience in investing in these products with over 40 transactions.

For the above reasons, the complainant's complaint is in our view unfounded. Complainant's losses including unrealised losses are not due to the complexity or unsuitability of the products recommended but as a result of unforeseeable market movements (Market risk). Which risk was to an extent mitigated by the diversification provided.

(4) With regards to the Fourth Remedy which is based on a declaration and order for compensation in the amount of £444,716, including interest and the subrogation:

The Financial Services Arbiter should reject this demand on the basis that it does not have the competence to decide matters above the stipulated quantum of EUR250,000 and the loss suffered by the complainant was not due to the Company's negligence or misconduct but solely due to unforeseeable market movements known to the market in question.

(5) With regards to the Fifth Remedy which is that in the event that the monetary value of (i) above less than (iii) above is in excess of the amount competent to the Arbiter aware, the Hon. Arbiter shall recommend to the Respondent Firm to pay the complainant any balance in excess of such sum in terms of Article 21(3)(b);

The Financial Services Arbiter should reject this demand; as such order is discretionary and should be based on relevant evidence, which substantiates this demand.

(*6) With regards to the Sixth Remedy which is to declare and order the Respondent Firm to pay interest at a fair and reasonable rate for the period from 1st June 2011 and the date of effective restitution of the capital invested of £444,716, as per claim 4.i above;*

The Financial Services Arbiter should reject this demand on the basis that it does not have the competence to decide matters above the stipulated quantum of EUR250,000 and the loss suffered by the complainant was not due to the company's negligence or misconduct. No guarantee was ever given to the complainant that the investments being the subject of the complaint will pay back all that was expected of them. Such "automatic" guarantee does not exist at law.

11. That in view of the above, it is submitted that there could be no remedy to the Complaint as it is unjustified in fact and at law.

Considerations

The first preliminary plea states *inter alia* that:

'*in so far as the Complaint document itself is concerned the Company declares that the copious evidence submitted in this Complaint is inadmissible and should*

be struck off by the Arbiter as all documents submitted are irrelevant and in clear breach of Article 558 of Chapter 12 of the Laws of Malta which clearly states that "all evidence must be relevant to the matter in issue between the parties"'.[22]

[22] *A fol.* 362

The Arbiter rejects this plea on the grounds that the procedure before the Arbiter is not regulated by Chapter 12 of the Laws of Malta but by Chapter 555 which stipulates that the procedure is established by the Arbiter and, consequently, Article 558 of Chapter 12 is irrelevant and does not apply to proceedings before the Arbiter.

This legal position taken by the Arbiter in this regard has also been confirmed recently by the Court of Appeal.[23]

The Arbiter also wants to underscore that even the service provider has filed extensive documentation and lengthy submissions that not all of them might be relevant to the merits of the case.

This plea is being rejected.

The second plea states that the complaint is null and inadmissible and should be considered inadmissible in accordance with Article 159 of Chapter 12 of the Laws of Malta.

The Arbiter reiterates that its procedure is not regulated by Chapter 12 of the Laws of Malta; the complaint is clear and the service provider itself submitted a very long reply and, therefore, this plea is frivolous and is being rejected.

As to the third preliminary plea, the Arbiter observes that Chapter 555 of the Laws of Malta stipulates that the Arbiter can grant a remedy *which is binding* up to €250,000[24] but *"if he considers that fair compensation requires for a larger compensation'* he can '*recommend that the financial service provider pay the complainant the balance, but such recommendation is not binding on the service provider".*[25] The Arbiter will abide by these provisions of the law.

From these provisions of Chapter 555 of the Laws of Malta it is amply clear that the competence of the Arbiter for Financial Services is not capped at €250,000. For this reason this plea is being rejected.

Plea of Prescription

[23] ***Daniel Caruana et vs Crystal Finance Investments Ltd.,* 5/11/2018**
[24] Art. 21(3)(a)
[25] Art. 21(3)(b)

In this regard, the service provider submits that:

"*The complaint is time barred by the lapse of five years since the contractual relationship between the company and the complainant was concluded on 20 April 2011".*[26]

The Arbiter notes that the service provider did not specify the relevant Article of the Civil Code on which it is basing the plea of prescription. There is abundant jurisprudence which states that the party raising the plea of prescription must cite the specific section of the law. In the Court judgement delivered by the First Hall Civil[27] it was held that:

"*Illi f'dan il-kuntest jinghad li huwa principju llum stabbilit li jekk l-eccipjent ma jispecifikax liema preskrizzjoni qed jinvoka l-Qorti ma tistax tikkonsidraha u dan ghaliex altrimenti l-Qorti tkun qed tissupplixxi ghall-parti eccipjenti f'materja odjuza li fiha ma tistax tiehu inizjattiva (A.C. R. Cali vs Perit Galea - 11 ta' Mejju, 1956 - Vol.XL p.1 p.166); Air Malta p.l.c. vs Via Holidays and Travel Limited (P.A. (GV) – 29 ta' Jannar 2002) tant li fis-sentenza fl-ismijiet Henry P.Cole vs Salvatore sive Sammy Murgo (P.A. - 10 ta Lulju 2003) gie deciz:-*

'L-imsemmija l-ewwel eccezzjoni, rigwardanti l-preskrizzjoni, ma tista' qatt tigi akkolta, peress li l-konvenut naqas li jindika l-artikolu tal-ligi li fuqu huwa qed jibbaza din l-istess eccezzjoni tieghu.'

'Illi tal-istess portata hija s-sentenza Margaret Camilleri et vs The Cargo Handling Co. Ltd. (P.A. – 3 ta' Ottubru 2003) fis-sens li: 'Kwantu ghall-eccezzjoni tal-preskrizzjoni huwa principju assodat fil-gurisprudenza illi l-Qorti ma tistax ex officio taghti effett ghall-preskrizzjoni jekk din ma tigix eccepita mill-parti interessata f'forma specifika.'" Ara decizjonijiet a Vol.XXXIII P1 p481 u Vol. XLI P1 p178.)

The service provider did not indicate the specific Article on which it is basing the plea of prescription and this cannot be done by the Arbiter because in that eventuality he will be interfering in the dispute which militates against the very basic principles of impartiality. Furthermore, the service provider did not produce evidence to sustain this plea as it is obliged to do.

[26] *A fol.* 364

[27] *Paola Galea et vs John Cauchi et,* PA, 26.03.2010

For these reasons the Arbiter is rejecting the plea of prescription.

THE MERITS OF THE CASE

The Arbiter has to decide the complaint by reference to what, in his opinion, is fair, equitable and reasonable in the particular circumstances and substantive merits of the case.[28]

The complaint is about a portfolio made up of structured notes or index-linked products (both refer to the same type of product) which the complainant acquired on advice from the provider between April 2011 and December 2015. The complainant does not seem to have had a clear indication of the exact amount of products she had invested in during this period. In her complaint, she mentions "*circa 40 transactions*".[29]

The documentation appended to her complaint, and corroborated with further documentation by the provider, indicates that 35 structured notes were acquired over this period. This was eventually confirmed by the complainant in a subsequent submission (filed after the case had been adjourned for decision), when she listed all the products on a spreadsheet at the request of the Arbiter.

In total, between June and October 2011, the complainant transferred GBP408,001 and USD58,831 (in total GBP 444,716) to Nedbank, the custodian bank in Jersey, for investment purposes.[30]

According to a valuation statement issued by the custodian bank to the customer as at 30 June 2016,[31] the complainant's portfolio was made up of 10 of such structured notes which had not yet been called up and not yet matured, and was valued at GBP222,917. The value of the same portfolio as at 31 October 2016 stood at GBP269,507.[32]

During the hearing of 23 January 2017, the complainant gave a description of her profile, her attitude towards risks when investing, her previous investment experience as well as her relationship with the provider and its representative.

[28] Cap. 555, Art. 19 (3)(b)
[29] *A fol.* 63
[30] *A fol.* 58
[31] *A fol.* 202 et
[32] *A fol.* 392 et

The complainant said that she used to lecture on hotel housekeeping and train staff on the hotel industry and hotel management. Between 1988 and 2011, her income was derived from savings held with a bank in England.

As to her previous investments, she said,

"*Yes, I had approximately 300,000 in equities, 75,000 in unit trusts and funds and €60,000 in Barclays. I do not agree that I am a savvy investor. I never bought shares on my own; I always wanted somebody to guide me. I am not an experienced investor."*[33]

She claimed that her previous investments were not high risk.

"*I had a very experienced broker in England and he was investing in equities and bonds and I had a very good return on my investments. Any investment has risks, even money in the post office has risks. What I had in my portfolio was simple and straightforward. I could phone up my broker and ask questions; and it was straightforward. It was all very simple. But I'm afraid that Hollingsworth portfolio, I simply could not understand*",[34] the complainant said.

Later on, during re-examination, the complainant explained that her portfolio with her London stockbroker was discretionary.

"*Being asked whether I had any derivative-linked equities, I do not know what that means. I know the distinction between discretionary and advisory service",*[35] she said.

In regard to her risk attitude and the investments comprising her portfolio with the provider, the complainant stated:

"*My broker always took the decisions. When I answered about my risk attitude, I replied it was cautious to medium. When I invested, I did not know at the time that it was high risk. I realised that it was high risk when my portfolio started going down; from the portfolio reports that I received. When I asked Paul Tilbrook that my capital was going down, he said, 'Don't worry, you'll get your money back.'*

[33] *A fol.* 517
[34] *A fol.* 518
[35] *A fol.* 520

I never had these Structured Notes which were even more than high risk. I am saying this because my portfolio was examined by experts in England and I was told, 'You might as well have played them at the casino or betted them on the horses.'"[36]

As to the reasons which led her to lodge a complaint, the complainant said:

"*I consider that Hollingsworth were unprofessional because I lost my capital. I had a 5-year relationship with Hollingsworth. I am asked why I am complaining now, I say that because I have lost funds."*[37]

The provider, under cross-examination, stated that according to the complainant's Fact Find, she had experience in equities, unit trusts and bonds through the services of a U.K. stock broker.

"*I am being asked whether simple equities are not complex securities in terms of MiFID regulations, in my professional opinion, under MiFID equities are not deemed to be complex, but 91% of Mrs. GJ's portfolio consisted of equity type of products that contained equities. On each occasion that she invested, it was stated in writing, (in a letter that I composed and signed), that these instruments were deemed to be complex in nature; so I outlined to her, after investing for a number of years, that she gained many years of experience in investing in complex instruments and that was reiterated to her in writing, giving her the opportunity to question what that meant if she did not understand, or whether she had any questions,*"[38] the provider said.

In regard to the complainant's portfolio, the provider said:

"*Being asked whether the investments Ms. GJ had with our company were aggressive investments, I say that index-linked products are not aggressive.*

In my opinion, her portfolio was not high risk; it was a balanced portfolio. The complaint before the Arbiter is about her complete portfolio with us. I confirm it was a balanced portfolio. I confirm that it was not a cautious portfolio.

[36] *A fol.* 518
[37] *Ibid.*
[38] *A fol.* 520

Being asked by the Arbiter how was the portfolio balanced, I say Ms. GJ wanted to exit her bank deposit and knowing she had an equity with another stockbroker, with that knowledge over many years, we developed a balanced portfolio. It was a diversified portfolio."[39]

The provider confirmed that the complainant made a loss on her investments:

"*Being asked whether, in total, Ms. GJ made a profit or loss with the investments at Hollingsworth, I say the native fact: unfortunately, despite the majority of them being successful, she made a loss."*[40]

The Complainant's Investment Mandate

The mandate that the investor gave to the provider when advice was provided needs to be analysed in the context of the latter's obligations to act in the best interest of the client and to render a service, including recommendations of investments suitable for her requirements.

The Client Fact Find ("CFF") and the Personal Recommendation Report ("PRR") provide important information in this regard.

When providing investment advice, financial providers are required,[41] among other obligations, to obtain information from potential clients to enable them understand facts about their client and that, when recommending a specific transaction, the following criteria are satisfied:–

- *it (i.e. the investment) meets the investment objectives of the client;*
- *it is such that the client has the necessary knowledge and experience to understand the risks involved in the transaction and*
- *it is such that the client is able to financially bear any related investment risks consistent with her investment objectives.*

A **Client Fact Find ("CFF")** was compiled and prepared by Paul Tilbrook on 20 April 2011.[42]

[39] *Ibid.*
[40] *A fol.* 521
[41] SLC 2.16 *Assessment of Suitability* - Part BI: Standard Licence Conditions
[42] *A fol.* 497 et

In his affidavit,[43] Mr Tilbrook recalled meeting the complainant in April 2011 and confirmed that at that meeting, the complainant had informed him of her experience with different investments and that she *"already had a stockbroker who used to advise her on financial instruments consisting of bonds, shares and high risk investments."*[44]

In her affidavit,[45] the complainant claims that she had advised Mr Tilbrook that her investment attitude in regard to the portfolio that she asked the provider to manage was cautious or medium. Earlier, in the same affidavit, the complainant said that when meeting Mr Tilbrook, besides discussing her financial situation and objectives, she had clearly stated that her risk attitude was cautious, a claim which Mr Tilbrook denies.

"*There cannot be anything farther from the truth to this statement",* he countered in his affidavit.*[46]*

The complainant's primary concern was the safety of her money held in banks and that she stressed capital protection. The last thing she wanted was to substitute her bank deposits with financial instruments that had higher risks or difficult to understand.[47]

The purpose of the CFF[48] is for the provider to record important details of the prospective investor, including details about current assets (cash, moveable and

immoveable property) holdings as well as liabilities, previous investment experience and knowledge and, very importantly, its financial objectives and risk profile.

The CFF compiled by Mr Tilbrook denotes that, excluding the value of her home (denominated in euro) and an amount deposited with a bank (denominated in USD), all other investments and bank deposits were held in GBP, of which *circa* 60%, were held with five different banking institutions. Around 40% were invested in GBP-denominated investments, mainly unit-trusts and shares.

[43] *A fol.* 510 et
[44] *A fol.* 512
[45] *A fol.* 386 et
[46] *A fol.* 512
[47] *A fol.* 387
[48] *A fol.* 497 et seq.

The complainant expressed the wish to invest over the long term and the purpose was "*Capital Growth – no need for an income as pension income is sufficient. No dependents either".* Her investment attitude is indicated as "*Medium*". The *Client Confirmation* page[49] was signed by the complainant and the provider on 27 April 2011.

Following compilation of the CFF, an *Assessment of Suitability* and *Recommendations*[50] was also drawn up. Under this latter section, the financial provider summarises key aspects contained in the Fact Find and acknowledges that:

"*[she] is aware of the risks of investing in equity type investments. Her new portfolio will be designed to include mainly structured products that have defined risk parameters as opposed to holding more open-ended equity shares/products."*

It is observed that a copy of the CFF, with the Assessment of Suitability and Recommendations, had not been provided to the complainant at the initial stages of her professional relationship with the provider.

"*I am not aware that it is a regulatory requirement to give a copy of the document to the client but she signed the document at the office*",[51] the provider said.

As stated earlier, the financial provider also prepared a **Personal Recommendation Report ("PRR")** for the complainant, also bearing the date of 20 April 2011.[52] A copy of the PRR had been provided to the complainant.

Under section 2 of the PRR (Recommendations),[53] the financial provider observes that the complainant had confirmed that her present income was sufficient to cover for her everyday needs and that she sought advice to invest GBP220,000 and USD108,000 (this is struck out and a handwritten note in the margin indicates a revised figure of USD58,000).

[49] *A fol.* 502
[50] *A fol.* 504
[51] *A fol.* 520
[52] *A fol.* 121 *et seq.* (duplicate *a fol.* 405 *et seq*.)
[53] *A fol.* 407

"*As such you wish these cash reserves to be invested providing capital protection and also the opportunity for capital growth*".

The amount stated therein, in GBP, would have constituted around 20% of her total GBP net worth (excluding her home). **The amount invested was actually much higher than that.**

The recommendation indicates that the level of protection in regard to deposits held with one of the banks with which the complainant held deposits was only covered up to GBP85,000 per individual per institution and

"*For this reason it makes logical sense to move funds to a much more protected structure whilst still retaining your investment offshore status*".

The provider recommended as follows:

"*I have deliberately included a range of capital protected structures and funds that will provide you with more diversified portfolio than you presently hold. As new opportunities arise, we will suggest these to you and recommend that they become part of your overall investment strategy. Our role is to monitor each fund in the portfolio and recommend changes accordingly. This 'active management' principle means that changes can be made quickly and cost effectively."*

Section 4 of the PRR (Asset Allocation)[54] contains two sub-headings, both titled "*Capital Protected*".

Under section 5 (Additional information),[55] the advisor recommends half-yearly review meetings "*to discuss the development of your financial objectives*".

Analysis of the Investment Recommendation

In her sworn affidavit, the complainant said that the financial provider's recommendation in the PRR

[54] *A fol.* 124 (duplicate *a fol.* 408)
[55] *A fol.* 409

"*… was music to my ears because I logically understood this statement to mean that indeed HIFS would be investing my capital in a safer manner than the money on deposit in Guernsey and Isle of Man*".[56]

The complainant claims that, upon receipt of the report, she advised Mr Tilbrook that she would be relying on the financial provider's advice as she was not knowledgeable in finance and did not understand the mechanics of the instruments recommended.

Neither the CFF nor the PRR refer to any structured notes the complainant might have held previously. There are no indications that the complainant was knowledgeable and experienced in such investments. It is true that, in regard to a number of structured notes, the underlying investments were equities and that she held a portfolio of such securities with a UK stockbroking firm on a discretionary basis. But that does not render an investor knowledgeable of such structured notes simply because she had held a portfolio of equities.

The complainant confirmed that she had investment knowledge in shares, bonds and unit trusts and used to take interest in her portfolio and ask questions to her stockbroker. However, it results that her knowledge of investing did not extend itself to understanding the mechanics of the structured notes that were being recommended to her.

"*But I'm afraid the Hollingsworth portfolio, I simply could not understand*",[57] she said.

When considering the choice of investments recommended to her by the service provider, it is important not to lose sight of the very purpose she wanted to invest. It is evident that her main purpose for investing was not income but growth, but more importantly, the protection of her savings which were held in bank deposit accounts and which attracted a limited level of protection in case the bank in which she held funds was declared insolvent. "*Capital protection"* was, therefore, a primary consideration and of foremost importance.

Both the CFF and the PRR refer specifically to this aspect. However, the extent to which "*capital protection*" in the CFF is portrayed in regard to the structured

[56] *A fol.* 388, Paragraph no. 5
[57] *A fol.* 518

notes that the provider was recommending is different to that as described in the PRR.

Whereas in the CFF,[58] there is an indication that protection to capital was not full (by making reference to "*defined risk parameters*"), in the PRR, the element of protection is neither qualified nor explained. The key statement in the Recommendations contained in the PRR is this:

"*I have deliberately included a range of capital protected structures and funds that will provide you with more diversified portfolio that you presently hold*".[59]

The brief description for each Note in the PRR gives the impression that capital would be repaid in full on maturity. Indeed, the version of the PRR attached to the complaint (Doc C) includes handwritten notes, presumably made by the complainant, which reflect that she understood the term "*Capital protected"* to mean: "*will receive 100%*".[60] Unlike, the CFF, the recommendation in the PRR was reassuring.

It is not clear why, besides the PRR, the provider prepared a Recommendation in the CFF (that contains a truer description of such structured products than the PRR), but then did not hand over a copy to the complainant. The provider claimed that he was under no regulatory obligation to provide a copy of the CFF to the investor.

The Arbiter's view is that this is not as clear-cut as is being argued by the provider. The regulator's guidance notes,[61] which lay out a specimen Client Fact Find for the Suitability Test,[62] and which the provider has clearly adopted in both style and content, contains this statement under "*Client Confirmation*":

"***I/We confirm that I/We do/do not* require a copy of this document. *delete as appropriate***."

[58] A copy of which was only provided to the complainant until after she submitted her complaint.
[59] Emphasis added
[60] *A fol.* 124
[61] https:/www.mfsa.com.mt/pages/readfileaspx?f=/Files/LegislationRegulation/regulation/securities/investmentServices/Rules%20for%201SP/Guidance%20Notes%202320November%202007%20Consolidated.pdf
[62] Page 130 of the Guidance Notes issued by the MFSA

The provider did not reproduce this statement in its version of the Fact Find but rather took it upon itself to arbitrarily decide for its clients and amended the statement to read:

"***I Confirm that I do not require a copy of this document**."*

None of the index-linked products which had been recommended to the complainant were "*capital protected*" in the true meaning of the term and the manner in which a retail investor would have ordinarily interpreted it.

Structured Notes

Structured Notes, index-linked or equity-linked products, are financially engineered investments where the investor's return depends on the price performance of a so-called "*underlying*". The underlying could be a combination of equities or an equity index, or basket thereof. The risk/return characteristics of such products may not necessarily reflect the risk/return of the underlying.

The return to the investor consists of a payment depending on the performance of the underlying as specified in the terms of the product. Depending on the terms and conditions of the product, the payment on maturity of the initial nominal amount invested may be full or partial. Depending on the design of the product, some structured notes are "*capital protected"* (the payment of the initial amount is made in full on maturity) but others are "*capital at risk*" (where on maturity, the investor may not receive the original amount invested in full).

In the latter type, and by way of an example, a fall in the price or value of an underlying on maturity of a product by more than, say, 50% compared to the price of the same underlying at a particular interval, could trigger a reduction in the amount of payment to the investor by as much as the loss in price or value for that underlying.

A number of index-linked products that were advised to the complainant had an "*Autocall*" feature. A product with such a feature would be called by the issuer prior to maturity if the underlying is at or above its initial level (or any other predetermined level) on a specified observation date. The investor would receive the principal amount of their investment plus a pre-determined premium and the autocallable product is said to be redeemed early. A product

which has an "*Autocall*" feature might benefit from an early redemption if the value of an underlying is favourable on the basis of the product's design.

However, and depending on the product's design, the issuer would not be obliged to early redeem a product in the event of loss in price or value of the underlying. In such a situation, investor's risk is realised on the product's maturity depending on the value of the underlying.

None of the Structured Notes recommended to the complainant were "*principal protected*" but rather "*capital at risk*".

Structured notes have been classified as *complex instruments* by ESMA[63] (formerly CESR).[64] ESMA determined so when it was referring to the myriad of financial instruments falling under "*other forms of securitised debt*".

It stated, "*those that embed a derivative and those that incorporate structures which make it difficult for the investor to understand the risk attached to the product should be considered as complex products for the purposes of the appropriateness test*".[65]

Shares and bonds, unlike structured notes, are non-complex investments. Investing in a wide pool of investments consisting of shares and bonds, actively managed and monitored in line with changing market conditions would not possibly be considered akin to investing in a pool of structured products, such as those which the provider recommended, where there was absolutely no active management and hardly any monitoring as promised in the PRR.

As to portfolio diversification, unlike the claims made by the provider during cross-examination, neither was the asset allocation diversified nor "*balanced*".[66] A portfolio made up entirely of structured notes, similar to those described in the Asset Allocation, could not possibly be described as "*diversified*". A diversified portfolio would have been composed of a range of uncorrelated assets in varying proportions, selected in accordance with the

[63] European Securities and Markets Authority, formerly *Committee of European Securities Regulators*
[64] *A fol.* 310 *et seq. – MIFID Complex and non-complex financial instruments for the purposes of the Directive's appropriateness requirements (CESR/09-559, 3 November 2009).*
[65] *A fol.* 314 (Paragraph 37 of the CESR Q&A)
[66] *A fol.* 520

requirements of the investor and taking account of her risk and return preferences. The Asset Allocation was over-exposed to a class of index-linked products with limited capital protection aimed at professional/sophisticated investors.

Once invested, the provider had absolutely no control over the performance of any of the components of the complainant's portfolio. That holds true of any portfolio as the performance of a pool of investments is for the markets to determine.

But, the manner in which this particular portfolio evolved over a span of four years (2011 to 2015), is particularly telling. There was hardly any "*active management*"– a promise made by the provider in the PRR – but rather an investment strategy that remained passive throughout. Indeed, the provider itself confirmed that these products were meant to be held till maturity.[67] Selling the products before maturity could not guarantee that the price be more than that at which it was purchased.

The provider did not provide any details of any attempt it might have pursued at some stage to re-assess the suitability of the portfolio's composition in line with the investor's risk attitude.

Disclosure

Among other requirements, providers are required[68] to provide appropriate information in a comprehensible form to their clients, such that they are reasonably able to understand the nature and risks of the investment service to be provided and of the specific type of instrument offered. The purpose of this requirement is to ensure that the investor is able to take investment decisions on an informed basis.

Prior to each investment, the provider prepared a letter[69] addressed specifically to the complainant in which he would summarise the main characteristics of the investment being recommended. A fact sheet for the respective product was

[67] *A fol.* 567
[68] SLC 2.27 *Client Disclosure Requirements* - Part BI: Standard Licence Conditions
[69] *A fol.* 412, 413, 416, 420, 422, 428, 434, 437, 440, 445, 449, 451, 454, 457, 461, 464, 467, 470, 475, 477, 479, 481, 485, 489, 492 (these documents were provided by the service provider).

attached.[70] Some of these letters were endorsed by the complainant to signify her acceptance as to the recommendations.[71]

In some instances, the provider used to draw up an internal *File Note.*[72] Although the provider never met the complainant until April 2015, a number of these File Notes indicate that the provider held conversations or meetings with the complainant regarding the choice of investments he was recommending.[73]

The Key Information Documents (KIDs) contained detailed information about the products, the underlying, inherent risks and eligibility criteria.

The provider claimed that the designation on the KIDs referring to professional investors related to the distribution of the marketing material (i.e. the KID) and not of the underlying instrument.

The Arbiter has reviewed the KIDs presented in evidence and could notice that in all of these documents, on the first page and in similar prominence to the name of the product, a reference was always included that clearly and unequivocally spelt out for whom the notes should be offered.

Statements such as "*For eligible counterparties and professional clients only*" or "*For Professional Investors only, not suitable for retail distribution*" could not possibly have been included simply to satisfy a marketing requirement.

The product issuers included Nomura, Royal Bank of Canada, Insight and Commerzbank. The KIDs issued by these issuers varied in style and content, but however, each of these documents clearly highlighted common characteristics accompanying such products. If one were to take the Nomura documentation as an example, disclosure in regard to capital protection (or lack thereof) is clearly indicated. Likewise, as to who could purchase the Notes (Qualified Professional Investors, Offshore Life Companies buying as principal and Corporate and Institutional clients buying as principal).

[70] *A fol.* 127, 129, 131, 133, 135, 136, 140, 145, 147, 151, 155, 160, 162, 167, 169, 174, 176, 181, 184, 189, 191 (these documents were provided by the complainant)
[71] *A fol.* 462, 465, 468, 472, 476, 478, 480, 487, 491,494 (these documents were provided by the provider).
[72] *A fol.* 411, 415, 417, 421, 423, 430, 433, 438, 444, 446, 450, 452, 455, 459 (these documents were provided by the provider).
[73] Of the File Notes referred to above, only one made reference to a meeting being held between Paul Tilbrook and the complainant. *A fol.* 450.

The RBC (Royal Bank of Canada) Notes (of which the complainant held 18 products) also indicate that they were not capital protected (under "Risks") and that

"*This information is directed at sophisticated prospective investors in order to assist them in determining whether they have an interest in the type of securities described herein. In the UK it is directed only to those persons who are eligible counterparties or professional clients and must not be acted on or replied upon by retail clients.*"[74]

The KIDs were issued purposely for those investors who were eligible to invest in the product. It would have served no scope for an issuer to restrict distribution of such Fact Sheets to particular investor categories (such as professional investors) but then allowing the *actual sale* of such products to be unrestricted and open to retail investors. None of the Fact Sheets relating to the structured products recommended to the complainant were meant for retail distribution.

Conversely, if a KID for retail distribution was available, then the provider ought to have perused such documentation in regard to the complainant.

The complexity of such structured products rendered them risky for investors to the extent that they were meant to be offered to professional investors. The complainant, a retail investor, has shown that unlike her portfolio managed under discretionary basis by a UK stockbroker, she could not understand the products that the provider had recommended her.

The complainant neither had the capacity nor was she in a position to "*second guess*" the provider (and its representative) as she was entitled to rely on the advice she was being given.

The fact that the provider used to include a statement in the personalised letters to the complainant that the products were complex but that he still considered them to be suitable for the investor would not absolve the provider from his duty of care as required by the rules that, in providing a service to clients, it shall act honestly, fairly and professionally in accordance with the best interest of its client.[75]

[74] *A fol.* 130, for example
[75] *A fol.* 230 – SLC2.01 *Conduct of Business Obligations - Part BI: Standard Licence Conditions*

The complainant further claims[76] that she had never met the director of the financial provider prior to December 2015 (around the time she started expressing concerns as to the value of her portfolio). She did meet the provider informally at one stage at a social event which she described as nothing more "*than a cordial casual handshake*". The financial provider corroborated the complainant's statement.[77]

The financial provider confirmed that it was Mr Paul Tilbrook who had met the complainant in April 2011 at her house in his capacity of representative of the provider and not as a financial advisor.[78] The purpose of the meeting was to gather the required information for the provider to be able to prepare an investment recommendation.[79]

In any case, the necessary paperwork had been signed by the financial provider and the onus of responsibility for the conduct of service in regard to the complainant lies squarely on it.

The Portfolio's Performance – Developments following submission of the Complaint and adjournment for Decision

As stated earlier, the initial amount invested through the provider amounted to GBP444,716,[80] spread over five payments between June and October 2011. The provider has not disputed this amount. At the time, this investment amount constituted around 38% of the complainant's total wealth (excluding property). The remaining investments were in deposits (*circa* 24%) and a portfolio of equities managed by a stockbroker in the UK (*circa* 38%).

Until 1 August 2017, the complainant never withdrew income or capital from her portfolio.

Portfolio Valuation as at end of June 2016

[76] *A fol.* 388
[77] *A fol.* 521
[78] *A fol.* 506
[79] *A fol.* 116, Paragraph 10
[80] *A fol.* 58-59

In her complaint application, the complainant referred to her June 2016 valuation statement issued by Nedbank, the custodian bank in Jersey.[81] She explained that, out of 35 investments, ten had not matured and the market value for each of such investments was indicating a loss compared to the nominal amount invested.[82] One must point out that such loss was provisional because each of the said ten investments had yet to mature or "*Auto-called*".

Furthermore, according to the complaint application, the investor had realised losses in regard to six other investments,[83] but realised profits in regard to a further two.[84] Neither the complainant nor the financial provider submitted any details on the performance of the remaining 17 products (also comprising the same portfolio) which matured or were auto-called at some stage *prior to June 2016*.

The total portfolio valuation[85] as at June 2016 stood at GBP 222,917 (including any cash balances held in the same account). As the complainant had not withdrawn any funds from her investment account, had those losses been realised – that is, had the investor disposed of her remaining products at the prevailing market value and withdrawn the monies – she would have effectively made a loss of GBP221,799 or around 50% on her original capital amount invested. According to the complainant, this provisional loss as at 30 June 2016 was the summation of realised losses and profits on eight products and unrealised provisional losses for the ten other products which had yet to mature or "*auto-called*".

As remedy to her complaint,[86] the investor requested that she is reinstated to her former financial position, that is, putting her back to the same financial position she was in prior to investing GBP444,716, through the services of the financial services provider, with interest and, simultaneously, transferring the legal and beneficial title in the Portfolio Number 763309, held in custody by

[81] *A fol.* 202 to 208
[82] *A fol.* 65, Section 3.5
[83] *A fol.* 64, Section 3.2
[84] *A fol.* 68, Section 3.4
[85] *A fol.* 204
[86] *A fol.* 98

Nedbank in Jersey, together with subrogation, in favour of the provider for all residual rights in the same investment, including litigious rights.

Portfolio Valuation as at April 2018

On 19 April 2018, after the case had already been adjourned for decision and the complainant and financial services provider had lodged notes of final submissions,[87] the latter filed an application[88] in the acts of the complaint that was primarily meant to give an update in regard to the portfolio value of the complainant's investment account and to challenge the complainant's pleaded sum of £444,716 in compensation.

The provider made special reference to the provisional estimate of losses allegedly suffered by the complainant which, on a portfolio valuation of GBP222,917 as at 30 June 2016, was estimated at GBP221,799. The provider objected[89] that a claim for compensation should be based on "*unrealised losses"* as the sum had not been lost or crystallised. The provider added that the valuation as at June 2016 had "*substantially altered due to the very nature of financial instruments and market fluctuations*".

To corroborate such assertion, the provider annexed a valuation statement issued by the custodian bank as at 31 May 2017, which the provider claimed had been brought to its attention after the case had been adjourned for decision. According to this valuation statement,[90] the portfolio valuation of eight products and cash held in account, amounted to GBP303,796. The provider claimed that, therefore, "*unrealised losses*" amounted to GBP140,920 (GBP444,716 less GBP303,796).

The provider explained that since lodgement of the complaint, six of the ten products which were still outstanding (as at June 2016) had matured and the complainant enjoyed positive returns in regard to five products. It went on to list these six investments, indicating whether capital was returned in full and the amount of profits paid. In regard to the remaining four – which had not matured

[87] The complainant's note of final submission was dated 6 April 2017 (*a fol.* 526 *et seq*.), and that of the provider was dated 18 May 2017 (*a fol.* 564 *et seq*.)
[88] *A fol.* 580 *et seq.*
[89] *A fol.* 581, Paragraph 4(d)
[90] *A fol.* 587, 588

or been auto-called – the provider gave its own assessment of how each investment was likely to fare based on current market performance.

On this basis, the provider claimed that the original value of "*unrealised losses*" ought to be revised downwards in view of positive performances which had been realised for six products and likely to be realised in regard to the remaining four.

On 26 April 2018,[91] the complainant submitted a response to counter the provider's claims. On reintegrating her original position prior to the investment, the complainant claimed that none of the parties to the dispute would be prejudiced through the mechanism of restitution. Should the loss in value of the investor's portfolio - valuated by taking the value at time of the complaint and that at which the service provider pays back the net capital invested - were to diminish, then that would imply that the value of the portfolio that is transferred to the service provider beneficially will have increased in value compared to that when the complaint had been submitted.

In support of this argument, the complainant referred to the portfolio valuation as at end March 2017, which showed a market value of GBP292,048, a provisional loss of GBP152,668,[92] compared to the amount invested of GBP444,716.

The value of the complainant's portfolio continued to improve and as at end July 2017,[93] the market value stood at GBP325,268 (which included an accumulated cash balance in favour of the complainant amounting to GBP187,098). In the meantime, more investments matured or were "*auto-called*" by the respective issuers.

The complainant revealed that on 1 August 2017, subsequent to the filing of the complaint in September 2016 and after the case had been adjourned for decision, she withdrew a capital sum of GBP160,000 and USD20,000

[91] The response was originally submitted in the Maltese language on 26 April 2018 (*a fol.* 597 *et seq*.) but, following the Arbiter's decree of 9 May, an English version was tabled on 14 May 2018 (*a fol.* 626 *et seq*.)
[92] The market value of the portfolio as at end June 2016 stood at GBP222,917, a loss of GBP221,799. See *a fol.* 64.
[93] *A fol.* 609 *et seq.*

(equivalent to GBP15,267 at a rate of exchange USD/GBP 1.31) from her cash account which formed part of the Nedbank portfolio.

The reason behind the withdrawal of this amount has been explained as follows:

"*The Complainant – who in the meantime had to undergo a series of surgical operations which she required to pay for and who also wanted to earn some interest on the idle cash balances by investing them in prudent and cautious investment grade £Stg bonds and thus further minimise the quantum of damages she is claiming by way of lost income on the capital loss she sustained due to the investment misselling of defendant company – on 1st August 2017 withdrew a capital sum of £Stg160,000 and US$20,000. The rate of exchange between the US$ and the £Stg as of the 1st August 2017 was 1.31, and therefore the US$20,000 had a £Stg counter-value of £Stg15,267. Therefore, the net capital invested by Complainant in the Portfolio which was exclusively managed by the defendant company was down from the previously sum of £Stg444,716 to £Stg269,478 on 1st August 2017.*"[94]

The complainant provided a further update to the portfolio valuation.[95] As at 31 March 2018, the total value of the portfolio (comprising a cash balance) stood at GBP167,130.93. As at that time, only four investments had yet to mature or be auto-called.

Subsequent to this Reply, a sitting was held on 29 May 2018, during which the Arbiter requested the complainant to provide a detailed breakdown of any profits or losses earned or incurred for each of the investments comprising her portfolio.

On 5 June 2018,[96] the complainant filed an explanatory note and attached a spreadsheet showing a detailed breakdown of the performance of each of the 35 investments, of which 31 had matured or been auto-called by the end of March 2018.

[94] *A fol.* 629, Paragraph 5
[95] *A fol.* 615 *et seq.,* Document marked "*Dokument X*"
[96] *A fol.* 632 *et seq*.

By referring to the March 2018 portfolio valuation,[97] the complainant revised downwards the amount by which she was claiming compensation from the financial services provider.[98] The revised compensation figure was now GBP176,880,[99] compared to GBP444,716 (the original amount invested).[100]

This revised figure has been calculated by deducting the cash balance held in the portfolio account (GBP92,598) from the net capital invested (that is, GBP444,716 less the amount of capital withdrawn in August 2017). Simultaneously, with the payment of "*the restitution of a net sum of £Stg176,880*", the complainant would transfer the beneficial ownership of the four remaining products in favour to the financial provider, which had a market value of GBP74,532. As an alternative to the transfer of investments, the complainant offered to "*irrevocably engage to transfer the eventual maturity proceeds to Respondent Firm*".[101]

The net compensation amounting to GBP102,348 (that is derived by deducting GBP74,532, which is the market value of the remaining investments from GBP176,880, that is, the revised compensation figure) corresponds to that featured in the spreadsheet[102] which nets off interest earned on the various products from the total of realised and unrealised profits and losses of the 35 products (arrived at by deducting the Sales Value from the Book Cost).

On 9 July 2018,[103] the financial services provider filed a Note of Reply to that filed on 5 June 2018 by the complainant.

The financial provider referred, among other aspects, to the list[104] of investments providing details of the performance of 35 investments which comprised the complainant's portfolio, of which only four remained outstanding.

The financial provider claimed that:

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[97] *A fol.* 615
[98] *A fol.* 633
[99] *A fol.* 633, Paragraph 5(i)
[100] *A fol.* 98
[101] *A fol.* 633, Paragraph 5(ii)
[102] *A fol.* 634
[103] *A fol.* 638 *et seq.*
[104] *A fol.* 634

"*Albeit the fact that this is something that the Complainant ought to have done if at all during the documentary evidence stage of the proceedings, the Complainant's position in this Note is once again incorrect(!) and downright deceitful as elaborated below, which deceit further evidences the bad faith and flawed basis of the Complaint.*"[105]

The provider rejected the complainant's claim that 25 out of the 31 products that matured or had been auto-called resulted in a loss.

"*In actual fact, nine (9) out of thirty-one (31) investments did not mature successfully thereby resulting in a loss (which loss is in any case not attributable to the Defendant).*"[106]

In support of the provider's claim, a marked replica of the spreadsheet lodged by the complainant was attached to the Note of Reply[107] in which 16 investments are highlighted. The service provider claimed that, according to the spreadsheet, these 16 products, which were never referred to previously by the complainant, allegedly all resulted in a "*realised loss*" of £140 or £125.

The service provider explained that:

"*In actual fact the sum of £140 represents an amount equal to the dealing charge applied by the custodian, Nedbank. This is not an investment loss. Secondly, not only did these 16 products not suffer a loss but the vast majority either made a capital gain or income which has been factored in separately.*"[108]

The provider claimed that by including safe custody and transaction costs incurred by the custodian Nedbank was intended to overstate the alleged losses.[109]

The provider explained that there were further developments in regard to the remaining four investments. According to the provider, a further investment[110] had matured in July 2018 with full capital return plus interest. Therefore, three

[105] *A fol.* 639
[106] *Ibid.*
[107] *A fol.* 641
[108] *A fol.* 639, Paragraph 4(a)
[109] *A fol.* 639, Paragraph 4(c)
[110] Commerzbank AG GBP 03/07/18

investments remained outstanding. However, the service provider did not prove such allegation.

Observations relating to the Quantum

The replies and counter-replies which have been exchanged following the Application lodged on 19 April 2018 by the service provider contain substantial information as to the performance of the investments comprising the portfolio.

It is a serious shortcoming on the complainant's part not to have informed the Arbiter of the substantial cash withdrawal from her portfolio in August 2017. At no stage of the proceedings had the complainant expressed any desire or intention to withdraw any funds from the said portfolio, so much so, that in its claim for compensation as submitted in her complaint application, she requested the sum of the original amount invested with a simultaneous transfer of all legal and beneficial title of the assets comprising her portfolio together with a subrogation in favour of the provider for all residual rights in the same investments. The withdrawal of funds from the portfolio constituted a material fact which ought to have been notified immediately to the other party, apart from seeking prior authorisation from the Arbiter given that the case had been adjourned for decision.

The Arbiter has analysed the applications, replies and documentation tabled on 19 April 2018, 26 April 2018, 5 June 2018 and 9 July 2018, and will be taken into consideration when deciding the amount of compensation.

The Juridical Context

The Arbiter has to decide the complaint by reference **"*to what, in his opinion, is fair, equitable and reasonable in the particular circumstances and substantive merits of the case*".**[111]

As has been amply detailed above, it is evident that the advice that had been given by the provider to the complainant in 2011 was not in her best interest[112] and that it failed to act with due skill and care when recommending a portfolio

[111] Section 19(3)(b), *Chapter 555 of the Laws of Malta*
[112] SLC 2.01

exclusively invested in structured notes that had limited protection, contrary to what she wanted.

The provider failed in his fiduciary obligations towards the complainant in that not only did he recommend products which were unsuitable for her circumstances, but that the advisory procedures he adopted were unorthodox and certainly not the standard expected of a licensed, professional financial provider.

The provider failed to draw up a diversified and balanced portfolio of investments suitable for an octogenarian who wanted to preserve her capital.

Instead, the provider preferred to advise on a pool of 35 structured notes without taking account of basic notions of diversification, asset composition and risk mitigation commensurate with a medium risk attitude as expressly stated in the investor's Client Fact Find.

The provider mis-represented the risks inherent in the structured notes – all complex products - that he recommended to the investor in the PRR; besides offering these same products to a retail investor when it was clearly evident that the products were aimed towards professional or sophisticated investors as clearly labelled on the marketing documentation.

It is clearly evident that, in providing the advice and selling this investment to the complainant, the service provider infringed various Investment Services Rules issued by the MFSA to licence holders as clearly indicated above.[113]

Since the enactment of Cap. 555, these rules do not serve only regulatory purposes. The Act stipulates that in carrying out his functions in deciding the case, the Arbiter shall:

"*consider and have due regard, in such manner and to such an extent as deems appropriate, to applicable and relevant laws, rules and regulations, in particular those governing the conduct of a service provider, including guidelines issued by national and European Union supervisory authorities, good industry practice and*

[113] SLC 2.01; SLC 2.16 and SLC 2.27 of Part BI: Standard Licence Conditions.

reasonable and legitimate expectations of consumers and this with reference to the time when it is alleged that the facts giving rise to the complaint occurred."[114]

The non-observance of the Investment Services Rules issued by "*the national supervisory authority (MFSA)"* are of material importance for the Arbiter to decide whether the complaint is equitable, just and reasonable because, being based on the MiFID Directive, they are intended to regulate the conduct of business of service providers in the financial services sector to give investors a degree of protection.

Moreover, the service provider has failed to follow good industry practices and did not fulfil the reasonable and legitimate expectations of the consumer.[115]

The service provider wrongly advised the complainant when it mis-sold a pool of 35 structured investment products which were unsuitable to her.

The provider's behaviour was in breach of his contractual obligations towards the complainant.

For the above-stated reasons, the Arbiter decides that the complaint is fair, equitable and reasonable in the particular circumstances and substantial merits of the case in so far as it is compatible with this decision.

Compensation

In this case, the complainant ought to be paid the losses she sustained.

The final figures proving the losses sustained by the complainant are those referred to in the document on page 634 of the proceedings. The service provider states that there were sixteen investments that were never mentioned by the complainant.[116]

However, from the documents filed with the note of the service provider of the 20 December 2016,[117] it results that these investments were indeed made by the service provider on behalf of the complainant. The list of investments filed by the complainant, on page 634 is therefore correct in this respect. The figures

[114] Cap. 555, Art. 19(3)(c)
[115] *Ibid.*
[116] *A fol.* 638-641
[117] *A fol.* 399

mentioned in this note are not contested by the service provider with the exception that the service provider holds that the "*dealing charges*" of £140 or £125 levied on these investments should not be considered as losses suffered by the complainant.

The Arbiter does not agree with this reasoning, and once the Arbiter has decided that *inter alia* there was misselling of financial products, the complainant should as much as possible be compensated for her losses including "*dealing charges*" which were, in fact, paid by the complainant.

Regarding the losses suffered by the complainant, these should not include the sum of £20,895,[118] described by the complainant as "*unrealised capital losses*"[119] because the complainant **did not produce solid proof** that the value of these investments cannot appreciate in the future.

Each case has to be decided on its own merits, and during these proceedings the service provider indicated that certain investments complained of did appreciate in value. To award "*unrealised losses*" the Arbiter has to be morally convinced that the investments are in such a predicament that they cannot recover, a proof which has not been provided by the complainant in this case.

The Arbiter considers the losses sustained by the complainant as follows:

The actual losses suffered by the complainant amount to £81,452. The Arbiter has arrived at this figure by deducting the sum of £71,814 (being interest credited on the various products to the portfolio bank account as indicated by the complainant) from the sum of £153,266,[120] (being the sum of actual total losses).

Consequently, in accordance with Article 26(3)(c)(iv) of Chapter 555 of the Laws of Malta, the Arbiter orders Hollingsworth International Financial Services Limited to pay the complainant the sum of eighty-one thousand, four hundred and fifty-two British Pounds (£81,452), or their equivalent in Euro, in accordance with Article 21(3)(c) of Chapter 555 of the Laws of Malta.

[118] *A fol.* 634 (22,236-1,341= 20,895)
[119] *A fol.* 633
[120] *A fol.* 634 (207,657-54,391=153,266) (153,266-71,814=81,452)

With legal interest from the date of this decision till the date of payment.

The four investments which have not yet matured are to be kept by the complainant without prejudice to any legal remedies she might have at the date of maturity.

The costs of these proceedings are to be borne as to one-fifth by the service provider and four-fifths by the complainant.

Dr Reno Borg
Arbiter for Financial Services