

Ombudsman Determination

CIFO Reference Number: 16-000223

Complainant: [The complainant]

Respondent: [Company X]

It is the policy of the Channel Islands Financial Ombudsman (CIFO) not to name or identify complainants in any published documents. Any copy of this determination made available in any way to any person other than the complainant or the respondent must not include the identity of the complainant or any information that might reveal their identity.¹

[The complainant] complained that distributions had been made by [Company X] to a third party without [the complainant's] authorisation.

Background

[The complainant] held a pension plan with [Company X] known as the [redacted for anonymisation purposes].

According to [the complainant's] representatives, funds were transferred out of [the complainant's] pension plan by [Company X] on two separate occasions without [the complainant's] authorisation. These transfers took place on 19 March 2015 and 7 April 2015.

£53,340.00 was transferred on 19 March 2015 and £52,351.62 was transferred on 7 April 2015. The total amount transferred was therefore £105,691.62.

[The complainant's] representatives informed CIFO that the transfer instructions to [Company X] were provided by fraudsters, rather than [the complainant], and submitted that [Company X's] actions constituted gross negligence.

First transfer: 19 March 2015

On 6 March 2015, [redacted for anonymisation purposes] member services administrator at [Company X], received an email purportedly from [the complainant]. The email was received from the email address [redacted for anonymisation purposes], which is an address that is confirmed to have belonged to [the complainant].

The email requested a withdrawal of £53,340 and for the funds to be sent to [the complainant's] bank account with [Bank Y] or to a separate third-party account. [The

¹ Financial Services Ombudsman (Jersey) Law 2014 Article 16(11) and Financial Services Ombudsman (Bailiwick of Guernsey) Law 2014 Section 16(10)

complainant's] representatives informed CIFO that [the complainant] did not send this email.

[Company X] replied to this email, asking for a signed letter to confirm the payment of £53,340. Later that day, the fraudsters – who purported to be [the complainant] throughout their repeated correspondence - confirmed that an original signed copy of the letter would be sent by post on the following Monday.

On 9 March 2015, the fraudsters emailed [Company X] again, attaching a scanned copy of the signed letter and saying that the original was in the post. [Company X] replied the same day to inform the fraudsters that the withdrawal request had been made to an incorrect entity; namely, [Company Y] rather than [Company X].

On 10 March 2015, the fraudsters contacted [Company X] for confirmation of receipt of their signed withdrawal request in the post. [Company X] replied a day later, confirming it had not been received.

On 13 March 2015, the fraudsters contacted [Company X] again for confirmation of whether the letter had been received. [Company X] replied in the affirmative and said that payment would be transferred to the “nominated [Bank Z] account.”

On 18 March 2015, the fraudsters contacted [Company X] again for an update regarding payment. [Company X] confirmed that the funds would be sent to the [Bank Z] account on 19 March 2015.

Second transfer: 7 April 2015

On 23 March 2015, the fraudsters submitted a further request for a withdrawal of £52,351.62.

On 24 March 2015, the fraudsters contacted [Company X] for a response and [Company X] confirmed the withdrawal instruction would be made and the funds transferred to the [Bank Y] bank account nominated by the fraudsters.

The fraudsters contacted [Company X] again for an update, and on 27 March 2015 he confirmed that he would email them when payment had been made to the [Bank Y] account. The fraudsters sent a confirmation email to this effect on 1 April 2015 but emailed again a day later asking why the payment was delayed. [Company X] replied, confirming that payment would be made shortly.

On 7 April 2015, [Company X] confirmed to the fraudsters that the payment would be made to the [Bank Y] account after a £50 deduction for a CHAPS (Clearing House Automated Payment System) fee.

Aftermath

On 1 June 2015, [the complainant] contacted [Company X] to make a transfer of £80,000 from his pension account and this was when the fraud was revealed. [The employee] reported the matter to his line manager at [Company X].

On 2 June 2015, [the complainant] wrote to the managing director of [Company X]. The managing director responded on the same day, advising [the complainant] that the necessary authorities had been informed.

On 19 June 2015, the managing director wrote to [the complainant] saying that [Company X] could not be held liable for losses incurred through stolen identity and suggested that [the complainant's] email account had been hacked. Therefore, [Company X] was not willing to reimburse [the complainant's] pension fund for the two amounts transferred to the fraudsters.

Representations made to CIFO by [the complainant's] representatives

In support of [the complainant's] claim that [Company X] had been negligent, his representatives raised a number of points. These included the observation that the withdrawals were paid by [Company X] to two separate UK-based bank accounts. As a resident [abroad], [the complainant] had always used [an overseas] bank account, held with [redacted for anonymisation purposes].

[The complainant's] representatives drew CIFO's attention to the fact that the two UK-based bank accounts were opened in different locations of the country – Yorkshire and Essex –which they considered [Company X] should have noticed when making distributions.

In addition, [the complainant's] representatives suggested that the emails sent by the fraudsters were littered with spelling mistakes and grammatical errors. They highlighted the unusual phraseology and stilted language of the fraudulent emails, as well as the general tone, style and formatting, which were inconsistent with [the complainant's] previous correspondence with [Company X]; for example, there was no header containing [the complainant's] address and contact details on the fraudsters' emails.

Furthermore, 24 hours prior to the first contact [Company X] received from the alleged fraudsters on 6 March 2015, [the complainant] had spoken to [Company X] and confirmed that he had no immediate intention to withdraw funds from the pension plan.

[The complainant's] previous pattern of withdrawals was to obtain his income entitlement in a single lump sum. This method was unlike that adopted by the fraudsters, who made two separate requests for funds within a matter of weeks.

[The complainant's] representatives also raised the concern that, at the time, [Company X] did not take steps to verify the authenticity of the payment instructions; for example, it was pointed out that since the fraud took place, [Company X] have followed up subsequent email instructions received from [the complainant] with a telephone call.

As a fair and reasonable resolution to the complaint, [the complainant's] representatives submitted that [Company X] should reimburse [the complainant] for the full amount transferred of £105,691.62, together with any interest accrued and bank charges incurred as a result.

Representations made to CIFO by [Company X]

In response to the complaint, [Company X] asserted that the fraud took place as a result of [the complainant's] own actions in allowing his computer system to be breached. They made this claim because [the complainant's] personal email address was used by the fraudsters.

In support of this submission, [Company X] pointed out that two UK bank accounts in [the complainant's] name were opened at [Bank Z and Bank Y], which they assert could only have happened through access the fraudsters had to [the complainant's] personal documents stored on his computer. By [the complainant] not bringing the compromise of his computer and account details to their attention, [Company X] suggested that [the complainant's] actions contributed to the fraud subsequently perpetrated.

Findings

Reasons for CIFO dealing with this complaint

[Company X] has submitted that, in their view, CIFO is not an appropriate forum for the resolution of this complaint and that it should, therefore, be rejected.

I am of the view that there is no compelling reason why it is inappropriate for CIFO to deal with the complaint, contrary to [Company X's] assertion. The initial assessment of whether the complaint fell within CIFO's remit was considered by the case handler upon receipt of the complaint. After a letter was sent by CIFO to [Company X], notifying them of the complaint and requesting documents, [Company X] sent documents to CIFO and suggested that the complaint would be best dealt with through the courts. On 19 September 2016, the case handler responded to [Company X], saying that CIFO considered the complaint to be within CIFO's remit. He also asked for further documents relevant to the complaint which had not been provided by [Company X] in response to CIFO's initial request.

[Company X] have submitted that the initial mandate assessment by the case handler was not subject to any scrutiny. I note that the Ombudsman is able to delegate his powers as necessary in respect of the initial handling of complaints referred. In any event, CIFO's processes allow financial services providers to put forward views on the eligibility of a complaint under CIFO's remit. In this particular case, [Company X] did so.

I am of the view that the subject complaint is an eligible complaint that is appropriate to be dealt with by CIFO in accordance with our statutory remit. [Company X] provided relevant financial services to [the complainant] from [jurisdiction 2]. [The complainant] is a represented individual bringing his complaint against [Company X] and is therefore an eligible complainant. The complaint satisfies the timing conditions: it was not brought prematurely before a complaint had been made to [Company X]; the event took place after 2 July 2013; and the complaint was referred to CIFO within 6 years of the event taking place.

The financial loss suffered by [the complainant] is below CIFO's compensation limit of £150,000. The facts of this complaint are clear and well-supported by the documents provided by both parties. Furthermore, the statutory basis of the Ombudsman's mandate in [jurisdiction 2], the [relevant legislation], permits the Ombudsman to make a determination based on what is fair and reasonable in the circumstances of the complaint. The creation of CIFO by the States of [jurisdiction 2] was to provide an accessible and independent alternative to the courts for financial consumer complaints which fall within CIFO's remit. Therefore, I do not agree with the submission by [Company X] that CIFO is not an appropriate forum in which to review [the complainant's] complaint.

[Company X] again raised the argument that CIFO is not the appropriate forum following my second preliminary determination. This final determination is based on the statutory powers set out in the legislation establishing a financial services ombudsman in [jurisdiction 2]. In reaching this decision, CIFO also took note of [jurisdiction 2] trust legislation and the views previously expressed by [Company X] regarding CIFO's jurisdiction.

Actions of [Company X]

The original email from the fraudsters of 6 March 2015 asked [Company X] to send the funds to a new bank account. [Company X] confirmed that they needed an original signed letter to confirm that the maximum entitlement was not required at the time. This letter needed to be signed and returned. It appears that it was signed and returned by the fraudsters.

[Company X] acknowledge that the signatures on the payment instructions were forged but submit that they acted in good faith throughout.

I found it noteworthy that £2,100 was requested from [Company X] in an email dated 29 April 2015 from the correct email address of [redacted for anonymisation purposes]. In this email, it was suggested that [the complainant] had valuables stolen while [abroad] and required £2,100 to "get back home". This email was responded to by [Company X] on the same day when they requested a telephone call "in relation to the [email]". Therefore, I note that a telephone call for validation purposes was sought by [Company X] before the fraud was uncovered on 1 June 2015 but, for some reason a call was not required in the case of the two fraudulent withdrawal requests on 19 March and 7 April 2015.

I acknowledge that the fraudsters' instructions came from [the complainant's] email address and that this was the same email address used on 1 June 2015. I further acknowledge that this might not have appeared immediately unusual to [Company X] or [redacted for anonymisation purposes], but the lack of effective validation of email transfer instructions is unusual and the internal process at [Company X] has since been amended to now require telephone validation and sign-off from the compliance department before distributions from client accounts take place. These processes were reviewed in June 2015. If this control system had been in place at the time the fraudulent transactions occurred, I consider it likely that the frauds could have been prevented.

Trust instrument - exculpation and indemnification clauses

[Company X] have drawn my attention to Clause 16.1 of the relevant Trust Instrument. According to [Company X], this has the effect of an Exculpation Clause and reads as follows:

“No Trustee (and where a body corporate is a Trustee, none of its directors officers or servants) shall be liable for any actions, claims or demands arising out of anything done or caused to be done or omitted by him...in connection with the [Pension Plan] and costs arising therefrom, except for a breach for trust arising from his own fraud wilful misconduct or gross negligence.”.

I acknowledge that [Company X] suggests this has the purported effect of excluding any claims made to CIFO by [the complainant] barring gross negligence; however, under the circumstances, given [Company X's] conduct which allowed the fraud to occur on two separate occasions, I am of the view that they would be unlikely to be able to avail themselves of the exculpatory clause. However, the test to be applied by CIFO is a different one and it is not necessary to address the issue of gross negligence.

The question for CIFO to resolve is whether it would be fair and reasonable for [the complainant] to incur the losses as a result of [Company X's] errors. The failure to implement proper checks, particularly when there was reason to be suspicious about the requests, leads me to conclude that it would not be fair and reasonable to allow [Company X] to escape liability for its errors.

I further acknowledge [Company X's] assertion that the clause is written in terms that are common and found in many trust deeds and in accordance with [jurisdiction 2] law. [Company X] suggests that, as a result, the Ombudsman should not ignore provisions of [jurisdiction 2] law in dealing with this complaint. However, the statutory mandate granted to the Ombudsman is also established through [jurisdiction 2] law and requires the Ombudsman to take a broader approach to complaint resolution, taking into account what is fair and reasonable in the circumstances of the specific complaint. The exculpatory clause does not exclude CIFO's remit from consideration of this complaint and from the application of CIFO's fair and reasonable in the circumstances test to the specific circumstances which gave rise to [the complainant's] complaint.

Clause 16.2 of the Trust Instrument was also drawn to my attention by [Company X]. It is an Indemnification Clause and reads as follows:

“The Trustees...are hereby indemnified out of the Fund to the extent permitted by law against any actions claims or demands arising out of anything done or caused to be done or omitted by them...in connection with the Scheme and all costs arising therefrom, except an act or omission which the Trustee concerned knew to be a breach of trust and which the Trustee concerned knowingly and wilfully committed or omitted as the case may be”.

[Company X] has submitted there has been no act or omission which it knew to be a breach of trust and which it knowingly and wilfully committed, so it is entitled to rely on this Clause. For the same reasons as I have noted above, I do not find it fair and reasonable

for [Company X] to indemnify itself out of the Fund for the costs incurred by [the complainant] due to [Company X's] own errors.

I have concluded that, in these circumstances, [Company X's] actions were poor and inconsistent with good practice when they failed to take into account the following factors before making the distributions:

1. Two UK-based bank accounts were opened in different locations of the country;
2. the emails sent by the fraudsters contained spelling mistakes, grammatical errors, unusual phraseology and stilted language;
3. the tone, style and formatting of the emails was inconsistent with [the complainant's] previous correspondence;
4. [the complainant] had previously and recently confirmed that he had no immediate intention to withdraw funds from the pension plan; and
5. [the complainant's] previous pattern of withdrawals was to obtain his income entitlement in a single lump sum. The fraudsters made two separate requests for funds within a matter of weeks.

I also note that, since the fraud took place, [Company X] have followed up subsequent email instructions received from [the complainant] with a telephone call.

I have, therefore, considered the exculpation and indemnification clauses but, based on the above factors, I do not conclude that it would be fair and reasonable for [the complainant] to suffer a financial loss of £105,691.62 as a result of the failure of [Company X] to exercise sufficient care and implement effective control systems to prevent the two unauthorised transfers of [the complainant's] pension funds to fraudsters.

Trust instrument – bona fide belief to entitlement

Clause 16.3 of the Trust Instrument reads as follows:

“The Trustees shall not be liable in respect of any payment to any person erroneously made by them in the bona fide belief...that the person was entitled to it and a receipt issued to the Trustees by the person shall be a good and sufficient discharge of the obligations of the Trustee.”

This Clause suggests that [Company X] may be exonerated from liability if it believed *bona fide* (in good faith) that [the complainant] was entitled to the funds and the payment was made accordingly.

I recognise that [Company X] believed that the recipient of the funds was [the complainant], rather than fraudsters. Nevertheless, given that I consider [Company X's] conduct in this matter was not reasonable and was inconsistent with industry practice, I

do not think it would be fair and reasonable for [Company X] to rely upon this clause to avoid responsibility in this matter.

Public policy considerations

I have also considered the public policy issues raised by [Company X] as reasons for CIFO not dealing with [the complainant's] complaint. These public policy issues are:

1. The fiduciary industry is at the core of [jurisdiction 2's] status as an international finance centre. Not allowing [Company X] to rely on the Exculpation and Indemnification Clauses will significantly impact the willingness or ability of parties to act as trustees.
2. It is a matter for [jurisdiction 2's] legislature or judiciary to depart from the current state of [jurisdiction 2's] law in deciding whether the Exculpation and Indemnification Clauses can be discounted.

With respect, the public policy considerations raised by [Company X], in my view, misinterpret the statutory role of an Ombudsman, which is to resolve complaints brought against financial services providers in accordance with what is fair and reasonable in all the circumstances. This authority of the Ombudsman to resolve complaints was granted by the [jurisdiction 2] legislature and is set out in [jurisdiction 2] law in the [relevant legislation].

[Company X] have also suggested that CIFO is an inappropriate forum within which to resolve this complaint and that there is a significant, doubtful point of law which prevents me from reviewing the matter. According to [Company X], the significant, doubtful point of law is [relevant legislation], which sets out how the terms of a trust may not relieve a trustee of liability for a breach of trust arising from his own fraud, wilful misconduct or negligence.

I have already considered this argument by [Company X] above and I am of the view that it would not be fair and reasonable for [Company X] to rely on this provision to the detriment of the complainant given [Company X's] fundamental failings in the circumstances.

Alleged contributory negligence by [the complainant]

Finally, [Company X] submits that [the complainant] was negligent in allowing his email account to have been breached.

In support of this submission, [Company X] pointed out that two UK bank accounts in [the complainant's] name were opened at [Bank Z and Bank Y], which they assert could only have happened through access the fraudsters had to [the complainant's] personal documents stored on his computer. By [the complainant] not bringing the compromise of his computer and account details to their attention, [Company X] suggested that [the complainant's] actions contributed to the fraud subsequently perpetrated. [Company X] submits any award made should take into account this contributory factor.

I am not persuaded by this argument. Email account take-over is a common problem and is not, in itself, evidence of negligence on the part of the account holder. The [jurisdiction 2] Financial Services Commission published a warning on 11 March 2015, the same period during which the first fraudulent transaction was being attempted, specifically highlighting the increased use of compromised email accounts to commit fraud in circumstances such as this. The [jurisdiction 2] Financial Services Commission warning advised businesses, including [Company X], that:

“When an instruction is received by e-mail, business should ensure that they verify those instructions via a telephone call to a party authorised to give instructions. This should occur whether the instruction is to change the details of a customer or to transfer funds to or from an account.”

In any event, I consider that [Company X] had been put on notice of the risk by its regulator and that even the most careful of customers can have their account defrauded.

Furthermore, a forensic IT report produced by a firm of IT security consultants for [the complainant] confirms that his email account was attacked by a “brute force attack” in order to compromise the password and gain access. The reasonability of the forensic IT report has been independently validated by a third-party data security firm at the request of CIFO. While I am not convinced that a brute force attack was the specific means of compromising [the complainant’s] email account, I am satisfied that, on a balance of probabilities, a compromise of his email account occurred and was the source of the information required to impersonate [the complainant] and carry out the frauds. There was evidence of sufficient information in the emails stored on the computer that would enable bank accounts to be opened in [the complainant’s] name.

I also note that there has been no evidence provided of contributory actions by [the complainant] to suggest either that he was responsible for allowing his email account to be breached, or that [the complainant] was involved in opening or using the bank accounts used by the fraudsters for receipt of the transferred funds. [Company X] had spoken to the actual [complainant] the day before the first email from the fraudsters requesting a withdrawal and a formal validation process after receipt of this fraudulent email could have averted the fraudulent withdrawals.

Based on the absence of effective control systems at [Company X] at the material time, and the lack of any persuasive evidence that [the complainant] somehow contributed to the loss, it would not be fair or reasonable in my view for [the complainant] to suffer financial prejudice as a result of the erroneous distributions. [Company X] should compensate him accordingly. I am of the view, therefore, that it would not be fair for [the complainant] to bear any of the loss incurred in the circumstances and consider [Company X] responsible for the full amount.

8% interest rate until the date of determination

In response to the second preliminary determination, [Company X] has suggested that applying a rate of interest of 8% is not fair or reasonable in the circumstances and that applying interest for the period from 1 June 2015 to the date of the final determination

has the effect of penalising [Company X] for the length of time taken for CIFO to issue its determination.

In awarding interest, CIFO seeks to ensure that complainants have not been financially disadvantaged in real terms by making the complaint; however, in most cases, the current low interest rates paid by banks and other financial institutions do not accurately reflect the losses incurred by complainants. In addition, the rates of interest complainants have to pay in order to borrow on an unsecured basis are generally higher.

Furthermore, the interest is not a penalty, but a reflection of the opportunity cost of the amount retained by [Company X] during the period when both [Company X] and CIFO considered the merits of this complaint and no compensation had been paid to the complainant. It remained open to [Company X], as with any respondent firm, to make payment to the complainant at any time during this process.

I also note that the 8% interest rate is used by the UK Financial Ombudsman Service and is consistent with the post-judgment interest applied by the [jurisdiction 2] courts.

Final decision

My determination is that I uphold this complaint.

[Company X] must:

1. Restore [the complainant's] pension account to the position it would have been in had the two fraudulent transactions not occurred [£53,340.00 and £52,351.62 recredited to the account to reflect the dates when the amounts were fraudulently withdrawn];
2. based on the valuation of [the complainant's] restored pension account as at 1 June 2015, withdraw £80,000.00 from the account leaving the remainder in [the complainant's] pension account with [Company X] [[Company X] shall inform CIFO and [the complainant] in writing of this remainder amount with 30 days of this determination];
3. immediately pay [the complainant] the £80,000.00 that he originally wanted withdrawn on 1 June 2015;
4. pay [the complainant] 8% simple interest on the £80,000.00 from 1 June 2015 to the date of this determination [calculated to be £18,726.58];
5. permit [the complainant] to withdraw or transfer the remaining funds from his pension account with [Company X], without fee or reduction except as may be required by lawful authority, within 90 days of this determination.

[The complainant] must confirm whether he accepts this determination either by email to ombudsman@ci-fo.org, or letter to Channel Islands Financial Ombudsman, PO Box 114, Jersey, Channel Islands JE4 9QG, by **4 June 2018**. The determination will become binding on [the complainant] and [Company X] if it is accepted by this date. If we do not receive an email or letter by the deadline, the determination is not binding. At this point [the complainant] would be free to pursue his legal rights through other means.

If there are any particular circumstances which prevent [the complainant] confirming his acceptance before the deadline of 4 June 2018, he should contact me with details. I may be able to take these into account, after inviting views from [Company X], and in these circumstances the determination may become binding after the deadline. I will advise both parties of the status of the determination once the deadline has passed.

Please note there is no appeal against a binding determination, and neither party may begin or continue legal proceedings in respect of the subject matter of a binding determination.

Douglas Melville
Principal Ombudsman and Chief Executive

Date: _____