

UK Regulator Extracts Compensation from Fund Operator and Parent

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On November 10, the FCA issued a [Final Notice](#) relating that Capita Financial Managers Limited (“**CFM**”) had agreed to pay investors £66m over the collapse of a circa £110m unregulated collective investment scheme called the Connaught Income fund.

The decision has garnered interest because the FCA faced political pressure to speed up its investigation into this matter. The decision demonstrates a willingness to provide meaningful compensation to end-investors. Further comment has centred on the fact that CFM was not charged any penalty over a public censure and that CFM’s ultimate parent, Capita plc, agreed to fund any shortfall. The decision has not been received without criticism, however.

CFM was the Operator of the fund for a large portion of the fund’s existence. It did not directly manage the fund and did not hold itself out as competent to manage the fund’s investments; a fund manager handled those functions. However, as the FCA authorised entity, CFM retained the primary responsibility for managing the fund’s investments.

The fund, among other things marketed as a “Guaranteed Low Risk Income Fund,” invested in high-risk loans. The fund had provided credit to a bridging loan firm which went into administration, and this appears to have been the catalyst for the collapse of the fund in 2012.

The FCA asserted a wide range of failures against CFM, including monitoring failures (among other things, breaches of loan-to-value guidelines, a lack of loan security checks, and not identifying loan rollovers or the recycling of loans), inadequate record maintenance, and a lack of follow-up on concerns that CFM itself had identified. These translated into breaches of FCA Principles relating to skill and care, and communication with clients, and thus into compensation for the end-investors. The decision arguably has certain flaws, however.

- **Lack of causation/ strict liability:** The decision hints at, but does not properly assert or establish, causation between the actions of Capita and the losses suffered by investors. While causation is not a necessary showing in decisions of this type, setting expectations of high compensation to investors without more fine-tuning of issues of cause-and-effect may

become problematic in future cases.

- **No fine:** The lack of a fine indicates significant political pressure to prioritise compensation over penalties. However, it is perhaps an unhealthy precedent if, as the level of compensation indicates, the FCA believed the facts revealed serious shortcomings.
- **Parent assumption of responsibility:** While the decision stated that the parent company had voluntarily become involved (as it had been in a prior case), and no criticism was made of it, there was no discussion of the basis of the parent company's liability.
- **Factual shortcomings:** Perhaps due to other ongoing investigations, the decision does not refer to facts, entities, or individuals that one would expect to be referenced, namely who and what caused the fund's collapse. There is evidently a large back story to this action which would provide context for the shortcomings identified.

In that light, the Final Notice that is, in essence, a catalogue of imperfections that are not tied to factual outcomes, and a large bill but no fine, may seem a rather arbitrary outcome with little value as precedent or deterrent. For all this, the Final Notice is a salutary reminder to responsible entities, such as Operators and Appointed Representatives, that the expected standards of monitoring and oversight are high.

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