Tax loss due to a structured product allegedly acquired without the client’s order

Topic: **Investment advice** Case number: **2019/10**

> The client claimed that he was an investor who was willing to take only modest risks. He wanted to invest an account balance of several million US dollars in fiduciary deposit investments. Instead and against his express wishes, the bank had invested 2/3 of his entire assets in a single structured product, which was risky and also had a negative tax impact on him. He complained to the bank and demanded that it reimburse him the difference between the after-tax profit of the desired fiduciary deposit investment and the structured product. The bank refused to pay compensation, claiming that the client had acquired this product after detailed consultations and handover of the product documentation. In the written investment advisory agreement, the client was informed that the bank did not provide tax advice. This contract and the product documentation expressly stated that customers must clarify the tax consequences of an investment themselves and, if necessary, consult a tax advisor. The customer did not agree with the Bank’s position and submitted the case to the Ombudsman. The Bank was also not prepared to make concessions in the ombudsman proceedings.

In the present case, the Ombudsman was confronted with the problem that the factual representations of the customer and the bank regarding the investment completely diverged. In the ombudsman proceedings, both parties stubbornly adhered to these and were not prepared to accommodate each other. The Ombudsman therefore had to close the case without success and issued a final decision in which he acknowledged the parties’ positions and arguments.

The Bank was able to rely on a signed client profile which identified the client as an experienced investor with the investment objective of “growth”, willing and able to take significant investment risks. According to the bank’s presentation, advisory discussions had been held with the client for tailor-made structured products after the interest rate conditions were too unfavourable for the fiduciary deposit investments originally requested. With regard to the advisory discussions, the bank could only rely on the statements of the client advisor. In the customer history, in which the customer contacts were recorded, there were entries about many, sometimes quite insignificant events. However, there was no entry on the alleged advisory discussions for the controversial investment worth several million US dollars, which surprised the Ombudsman. The structured product was renewed once after expiry. The bank took the position that the customer had received the product documentation and transaction receipts. The product was also evident in the securities account statements. It described the customer’s position as untrustworthy and assumed that the customer had merely sought reasons to subsequently pass on the unexpected costs to the bank after becoming aware of the tax consequences.

The fact that there was no evidence that the customer had explicitly agreed to the transaction spoke in his favour. There was no written consent, nor was there any contact note indicating that the transaction had been discussed with the client and that he had agreed to it. In addition, a contact note stated that he was averse to structured products. Furthermore, the original transaction documents on which the bank relied did not clearly indicate a structured product. Under these

circumstances, the Ombudsman considered that the bank could not have invoked tacit approval of the transactions after the documents had been delivered. When the product was renewed after its expiry, it was then clearly described as a structured product, which the customer did not object to. It would have been incumbent on the customer to reprimand the alleged errors with the necessary clarity as soon as they became known.

On the assumption that the banks presentation, which was disputed by the customer, was correct and that the customer had decided to purchase the structured product after a consultation, the Ombudsman then examined the customer's argument that the product should not have been recommended to him because it was harmful to his tax situation. The client argued that with a fiduciary deposit investment that would have generated the same return as the structured product, he would have had to pay around CHF 100,000 less tax. This was because the structured product, which was denominated in USD, was subject to differential taxation, unlike the fiduciary deposit investment, where only the interest income would have been taxed. He argued that a product with such a special tax feature should not have been recommended to him, at least not without a corresponding explicit reference to it.

The bank took the position that the investment advisory agreement clearly stated that it did not provide tax advice and that the product documentation contained a further indication that the customer had to clarify the tax consequences of an investment himself.

According to the Ombudsman, it is common practice for banks to provide actual tax advice only on the basis of specific agreements, usually through specialised departments, and usually for a fee. However, according to the general banking practice he has observed, investment advice is not limited to the various risks that may affect the market value and security of an investment product. Rather, it also includes indications of product-specific tax risks and the potential for earnings after tax, especially when a client makes a certain investment for the first time.

Even if no tax advice is owed on the basis of the contractual agreement, the Ombudsman is of the opinion that, based on the duty of care incumbent on it in the context of investment advice, a bank may not recommend any products which, irrespective of the client's individual tax situation, lead to avoidable tax burdens due to his tax domicile and which have a substantially negative impact on the achievable income after tax. Whether in the specific case in question the structured product was to be regarded as "tax harmful" in this sense remained controversial in the present case, however.

Since the bank made it clear that it was not prepared to make any concessions, the Ombudsman refrained from commenting on the amount of the claimed tax loss in his concluding letter and stopped his mediation efforts. In doing so, he once again expressed his astonishment to the bank that it was unable to clearly document the advisory discussion and the client's consent to such a large transaction. This was not conducive to the credibility of its presentation and ultimately led to the dispute causing a great deal of expense and the ombudsman procedure having to be terminated with an unclear result.

As in this case, the Ombudsman continues to regularly observe that, although investment advisory services are increasingly formalised in written contracts, the documentation of the advisory discussions based on these contracts is sometimes completely missing or insufficient in content. Such cases seem astonishing to him in view of the entry into force of the regulatory conduct rules and documentation obligations of the Financial Services Act FINSA.