

The complaint

Mr D complains that Seedrs Limited failed to disclose key information regarding an investment opportunity promoted through its crowdfunding platform. Mr D says this caused him a financial loss.

What happened

Seedrs is an equity-based crowdfunding platform that promotes investment opportunities by way of campaigns. Prospective investors can view information about a company and the details of the investment in these campaigns on the platform before deciding whether to invest. In return for their investment they receive equity in the company.

Mr D invested £3,500 into a company promoted through the Seedrs platform in November 2018. I'll refer to this company as "Company A". Company A raised just under £1,000,000 during this crowdfunding campaign in return for around 25% equity. Company A's pre-money valuation at this time was just over £2,600,000. The campaign was successfully crowdfunded in May 2019.

Company A launched another crowdfunding campaign in September 2019 through the Seedrs platform. Company A was looking to raise a further £350,000. This new campaign prompted Mr D to complain to Seedrs as the pre-money valuation of Company A had dropped to under £18,000. It also mentioned that Company A was looking for further funds in order for it to trade effectively.

Mr D complained to Seedrs in November 2019. In summary he said:

- Company A's campaign was not fair, clear and not misleading as it failed to disclose that Company A's auditor had expressed concerns, prior to the campaign, around its ability to continue operating and to meet its financial obligations.
- Seedrs failed to inform him that Company A intended to raise more equity in 2019 and the campaign didn't disclose all of Company A's existing debt and liabilities.
- Seedrs misled investors on the actual use of proceeds of the funds raised as Company A used these to fund its operational expenses in 2018 and 2019 as opposed to a marketing push in 2019.

Mr D said he wouldn't have invested in Company A had he known the above and so he felt Seedrs should refund him the money he'd invested.

Seedrs looked into Mr D's complaint but didn't uphold it. In summary it said:

- As set out in its due diligence charter, it checked any financial information included in the campaign against Company A's accounts, however, it didn't audit these accounts.
- It encourages investors to perform their own due diligence and noted that Mr D had requested further financial from Company A after he had invested.
- As an early-stage business that wasn't profit-making, it wasn't surprising that Company A would need successful fundraising in order to continue and added that,

given Mr D's experience as a sophisticated investor, his knowledge of the financial services industry and the risk warnings presented to him, it was sure that he would have been aware of this.

- Seedrs wasn't aware of Company A's intentions to raise further funding within the year. However, Seedrs risk warnings explained that it's expected that companies raising on Seedrs' platform will complete further funding rounds soon after an initial campaign.
- A disclosure form was completed by Company A confirming there were no loans outstanding to the company, including any overdraft fees and it did seek contractual warranties from Company A around its financial standing and disclosure of debt.
- The campaign stated the intended use of the funds was to conduct marketing activity, as well as other operational and growth activities. So Seedrs didn't agree that it had misled Mr D.

Mr D wasn't happy with the response he received from Seedrs, so he referred his complaint to this service for an independent review.

An investigator at our service considered Mr D's complaint but didn't think Seedrs had acted unfairly. In summary she said:

- Whilst the use of proceeds section didn't include much detail, she didn't think it was misleading. She noted that Company A campaign didn't say the funds would be solely used for marketing and it explained the plausibility of funds being used for ongoing expenses.
- She hadn't seen any evidence to suggest Seedrs ought to have known that Company A intended to raise further funds following the first campaign, but nevertheless, Seedrs had made Mr D aware of this possibility through its risk warnings.
- The campaign provided investors with information about revenue growth figures only which Seedrs checked as part of its due diligence process. The campaign didn't disclose any profit or loss information and Company A was never promoted as profit-making business.
- If Company A's financials were important to Mr D then he ought to have conducted his own due diligence on this. And added that the information relating to Company A's auditor's comments was freely available to the public before the campaign was launched.

Mr D didn't agree with the investigator's opinion. In response he said Seedrs had failed to disclose the following two key pieces of information which meant his investment in Company A was much riskier than he was led to believe:

- The auditors had already informed Company A's existing shareholders that Company A needed to successfully complete a fundraising exercise in the last quarter of 2018 to enable it to meet its liabilities, which indicated a material uncertainty about the company's ability to continue.
- Company A had significant existing liabilities, as evidenced by its 2017 balance sheet and its July 2018 management accounts (in which £370,000 was listed as being debt), which were not disclosed to investors as part of and during the campaign.

In response to Mr D's comments, the investigator explained that Company A's existing debt is different to existing liabilities. She said Company A informed Seedrs that there was no existing debt and informed it of the existence of two convertible loan notes.

As Mr D remains unhappy, the complaint has been passed to me to decide.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

Having done so, I don't uphold this complaint for broadly the same reasons as the investigator. I understand this will come as a disappointment to Mr D, but I'll explain my reasons why.

Regulatory framework

At the time of promoting Company A's investment opportunity, Seedrs was authorised and regulated by the FCA. The relevant rules and regulations FCA regulated firms are required to follow are set out in the FCA's Handbook of rules and guidance.

The FCA Principles for Business ("PRIN") set out the overarching requirements which all authorised firms are required to comply with. PRIN 1.1.1G, says "*The Principles apply in whole or in part to every firm*".

The Principles themselves are set out in PRIN 2.1.1R. The most relevant principles here are:

- PRIN 2.1.1R (2) "*A firm must conduct its business with due skill, care and diligence.*"
- PRIN 2.1.1R (6) "*A firm must pay due regard to the interests of its customers and treat them fairly.*"
- PRIN 2.1.1R (7) "*A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.*"

Seedrs was also required to act in accordance with the rules set out in the Conduct of Business Sourcebook (COBS). And the most relevant obligations here are:

- COBS 2.1.1R (1) "*A firm must act honestly, fairly and professionally in accordance with the best interests of its client.*"
- COBS 4.2.1R (1) "*A firm must ensure that a communication or a financial promotion is fair, clear and not misleading.*"

So before approving Company A's promotional material, Seedrs needed to satisfy itself that the campaign itself was fair, clear and not misleading. And it also needed to be satisfied that by approving the promotion and allowing its customers to invest in Company A, it would continue to be acting in its client's best interests.

In order to satisfy itself of the fair, clear and not misleading nature of the claims or assertions made in the promotional material itself, Seedrs would need to carry out reasonable checks. What these reasonable checks involve, or indeed what they might be in any given case, is something which is very much left to each provider to determine and would vary according to the particular circumstances. It's clear that it wasn't the regulator's intention to provide a set of tick boxes which needed to be completed for a promotion to be approved.

I've also borne in mind that the FCA said the following in its July 2018 consultation paper on loan-based ('peer-to-peer') and investment-based crowdfunding platforms:

"It is our view that it will be unlikely that a platform could argue that it has met its obligations under Principle 2, Principle 6 (PRIN 2.1.1R) and the client's best interests rule (COBS 2.1.1R), if it has not undertaken enough due diligence to satisfy itself on

the essential information on which any communication or promotion is based.”

Taking the above into account - I've firstly considered how Seedrs acted, focussing on how the investment in Company A was promoted.

Company A's financials

I understand Mr D feels Seedrs failed to disclose important financial information regarding Company A. Specifically, he says Seedrs ought to have made him aware that Company A had significant existing liabilities as evidenced by its 2017 balance sheet and its July 2018 management accounts.

Seedrs set out in its membership agreement the level of checks it would conduct on investee companies. This explained:

“9.2 Our Review and Approval. We have reviewed every campaign that you see on the platform (or, in the case of campaigns created by us, we have prepared the campaign), and we have approved its contents as of a specified date as a financial promotion for the purposes of the FCA Rules. This means that we have concluded that the information, taken as a whole, is “fair, clear and not misleading” as of such date, which in turn means that for factual statements we have reviewed evidence of their accuracy, and that for aspirational statements or statements of opinion or belief we believe they are phrased appropriately in light of their speculative or subjective nature.”

This was also made clear to Mr D directly in Company A's campaign:

“In approving this campaign, Seedrs has concluded that the information, taken as a whole, is “fair, clear and not misleading.” This means that for factual statements we have reviewed evidence of their accuracy, and that for aspirational statements we believe they are phrased appropriately in light of their speculative nature.”

Seedrs' membership agreement also made it clear that it doesn't provide any advice and again reinforces that it will only review what's contained within the campaign:

“9.3 No Recommendation; No Reliance on Other Information. Our approval of a campaign, as described in paragraph 9.2, does not mean that we are recommending that you make an investment in the business, that we believe the business is likely to be successful or that we take any responsibility or will in any way be liable to you if the business is not successful. The investment decision with respect to any investment through the platform is yours and yours alone. Other than what is contained in the campaign, we have not reviewed or approved any information about the business.”

Having looked at the campaign presented to Mr D, I can see that no factual statements regarding the profitability of Company A were given. As such, Seedrs wasn't required to conduct due diligence on the profitability of Company A. The only financial information provided in the campaign was that Company A had revenue growth from £171,000 in 2015 to £425,000 in 2017. However, this was caveated with an explanation that information was taken from unaudited management accounts. And I'm satisfied Seedrs were in receipt of these prior to promoting the campaign.

Seedrs' due diligence charter explained that it would disclose details of an investee company's outstanding debts:

“Outstanding debts

We require each company to provide details of any outstanding debts and disclose the details in the Campaign. Our standard agreements also contain a contractual commitment from the company not to use the investment proceeds of their fundraise for the purpose of paying off existing debts, unless this has been clearly been stated in the ‘Use of Proceeds’ section of their campaign.”

With this in mind, I've thought carefully about whether Seedrs should have disclosed the £370,000 listed as debt in Company A's July 2018 management accounts. Seedrs has confirmed that, in line with its due diligence process, it obtained a disclosure form signed by Company A to confirm whether it had any loans outstanding. I've seen a copy of this, in which Company A stated it had no loans or overdraft fees outstanding. Company A did, however, confirm that there were two convertible loan notes that it had issued prior to the campaign - totalling £350,000. I've also seen copies of these loan note agreements and can confirm that these funds were to be converted to equity as part of the fundraising round. As such, the loan notes did not represent debt to Company A which would have remained outstanding after the funding round. So I'm persuaded Seedrs didn't mislead Mr D by not disclosing details of the convertible loans as outstanding debt.

Mr D also says that Seedrs should have disclosed that Company A's auditors had informed Company A's existing shareholders that it needed to successfully complete a fundraising exercise in the last quarter of 2018 to enable it to meet its future liabilities. Whilst I accept that not including key information about an investee company can render a promotion misleading, I don't think that is the case here. Generally, investee companies that are looking to raise funds via crowdfunding are not yet profitable and rely on future fundraising to continue their growth. This risk was highlighted to Mr D in Company A's campaign:

“Given the nature and type of businesses presented on the Seedrs platform, it is possible that the business has very little cash remaining prior to receiving this investment, and the investment sought may be necessary for the business's on-going existence.”

The FCA said in its October 2013 consultation paper on regulatory approach to crowdfunding (and similar activities) CP13/13 that:

“Different firms employ different approaches to due diligence. We expect it to be clear to investors how much due diligence has been conducted and whether the investor should be conducting further research of their own.”

In Mr D's complaint, Seedrs had made him aware what checks it would conduct - confirming the accuracy of factual statements in the campaign. Seedrs membership agreement also made it clear that it wouldn't review anything not contained within the campaign. The campaign contained very limited financial information and, importantly, contained no information about Company A's profitability or level of debt, so I think Mr D ought to have been aware that Seedrs hadn't conducted due diligence on this. Seedrs has explained that it encourages investors to conduct their own research before investing, so if the financial stability of Company A was important to Mr D, I think he ought to have made his own enquiries or decided not to go ahead given the absence of any of this information in the campaign.

The company accounts which Mr D has referred to in his complaint were all readily available to investors in the public domain through the Companies House website. He could have also asked Seedrs or Company A directly for this information. I've seen that Mr D eventually did ask for this information once he began making enquiries around Company A's financials in around October 2019. But clearly this was some time after he had agreed to invest.

On a final note on the issue of the financials of Company A, I recognise that the two convertible loans only accounted for £350,000 of the £370,000 listed in Company A's July 2018 management accounts. Seedrs has explained that it wasn't required to disclose all debt to Mr D as it isn't obligated to provide potential investors with exhaustive financial information. However, I don't agree. Considering Seedrs due diligence charter said it would "*require each company to provide details of any outstanding debts and disclose the details in the Campaign*", I think it ought to have made Mr D aware in the campaign that Company A had around £20,000 debt. However, if it had, I don't think it would have made any difference to Mr D's decision to invest. Clearly £20,000 debt isn't a lot considering Company A's pre-money valuation at this time was just over £2,600,000 and it was raising close to £1,000,000. Also, I'm not persuaded the financials of Company A were so important to Mr D at the time of investing that it would have prevented him from investing.

Further fundraising

It's clear from the submissions from Mr D and Seedrs that it's disputed when Seedrs became aware that Company A intended to raise more funds on the platform. Mr D has referred Seedrs to information he had received through his enquiries with Company A in October 2019. Seedrs says Mr D referenced a communication Company A sent to Seedrs in July 2019, in which Company A sought Seedrs' consent to raise a further £600,000 in 2019. However, Seedrs says this doesn't prove it knew Company A wanted to raise further funds prior to the first campaign as this communication was sent after the initial campaign had closed in May 2019.

Whilst I've not seen any evidence to suggest Seedrs knew about Company A's intentions to further raise on the platform, I don't think I need to make a finding on this. I say this as Company A's provided a clear risk warning regarding the possibility of further funding:

"4. Dilution

Any investment you make in a business displayed on the platform is likely to be subject to dilution. This means that if the business raises additional capital at a later date, it will issue new shares to the new investors, and the percentage of the business that you own will decline."

The above was also explained under clause 10.4 of Seedrs' membership agreement and so I don't think Mr D was misled here.

Use of proceeds

Mr D says Company A's campaign was also misleading as it said Company A would use the funds raised for marketing purposes.

Company A's campaign provided a section on the use of proceeds. This explained the following:

"The new investment will provide marketing budget...Investment will also be used to ensure the company has adequate resource to manage the growing network and maximise revenues accordingly."

Whilst it's clear the campaign said Company A would use some of the funds for marketing, it also said funds would be used to ensure Company A had adequate resource. Seedrs has confirmed that it's come to light following the completion of the campaign, that Company A used most of the funds raised for operational reasons rather than solely on marketing. However, I can see from the email chains between Mr D and Company A from October 2019

that Company A did spend some of the funds raised on marketing. The campaign didn't say how much of the funds raised would be allocated to marketing and resourcing the company and so I don't think the information provided by Seedrs about the campaign was misleading.

If how much Company A was planning on spending on marketing was important to Mr D's decision to invest then again I would have expected him to have made enquiries into this before investing. However, he didn't contact Company A until after he had invested and so I'm satisfied he was happy to proceed with his investment without this knowledge.

My final decision

My decision is that I don't uphold Mr D's complaint against Seedrs Limited.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr D to accept or reject my decision before 20 January 2022.

Ben Waites
Ombudsman