DRN-3324796

The complaint

Mr D is represented by his lawyer. He seeks compensation for financial loss that he says resulted directly from Gain Capital UK Limited ('Gain') –

- Erroneously under-calculating and applying the margin required for US S&P 500 Options trades he opened between 3 March 2020 and 20 April 2020, all expiring on 16 May 2020 ('*the Options*').

- Failing to identify and notify him of this error until 21 April 2020, when margin for the Options was recalculated and increased, then failing to give him reasons until 23 April 2020.

- Failing to give him at least 24 hours notice prior to the margin being increased.

- Freezing his account immediately on 21 April and preventing him from mitigating his position through hedging.

Gain accepts responsibility for the erroneous margin calculation/application that affected the Options. One of our investigators upheld the complaint. She awarded Mr D compensation for financial loss (which Gain calculated to be £30,342) and she considered Gain's offer of £2,000 for the trouble and upset caused to him more than she would award for that purpose. Gain initially contested the financial loss compensation award, then it agreed to pay it. The matter remains in dispute because Mr H says the award does not cover all his financial loss.

What happened

Mr D's lawyer recently made submissions which helpfully summarise the background to the issues in dispute, and the issues themselves. In the main, the submissions said:

- Clause 10.4 of the terms agreed for his Gain account says Gain may change the margin requirement for trades, but clause 10.9 says in such circumstances Gain will provide at least 24 hours notice of any increase in the margin requirement.

- Gain, as a regulated firm providing the trading/trading platform service in the account, was also under the regulatory obligations to act honestly, fairly and professionally in his best interests; and to ensure communications with him were clear, fair and not misleading. ['*the regulatory obligations*']

- On opening the Options he had no knowledge, or cause to know, that the margin for them had been wrongly under-calculated.

- On 21 April Gain informed him that the margin had been revised and increased, and that he had insufficient margin in the account (the '*margin breach*'). No prior notice of the increase was given to him. Furthermore, his account was immediately frozen because of the margin breach – he could not open new trades – and the options he was given were to either fund the account to restore margin in it or to reduce his

open trading positions for the same purpose. Around £27,000 was required to fund the account and restore margin, he did not have such capital available and had to fund the account in instalments over time. He eventually completed the requisite funding of the account on 11 May 2020, the account was then unfrozen and he could resume trading.

- Despite its actions on 21 April, it was not until 23 April 2020 that Gain clarified to him that margin had been wrongly under-calculated for the Options at the outset, hence the revision and increase of margin. In between these dates, he was given limited and misleading information about the reason for the increase.

Mr D's position is that Gain's miscalculation of margin for the Options, its failure to give him at least 24 hours notice of the margin increase, the misinformation (about the reasons for the increase) it gave him between 21 and 23 April and its action in freezing his account immediately (preventing him from making mitigating hedge trades) all combine to establish serious breaches of the contractual and regulatory obligations it owed him. His lawyer says starting from 21 April and by the time he regained access to trading (on 11 May) the account had incurred a total loss of around £111,000 (including around a third of the money he had used to fund the account up to 11 May). This is the compensation amount Mr D is claiming, and is the reason why he considers the compensation awarded by the investigator significantly insufficient.

In terms of compensation, the investigator mainly said:

- Gain is responsible for the margin calculation error that affected the Options. For redress, an immediate consideration is what would have happened but for that error. Mr D has confirmed that the Options in the particular product had been opened following long-term planning and an informed trading strategy, so he would have traded the Options at the time in any case. He has also said that he would not have opened some of the Options if he knew of the real level of margin at the time. On this basis, it would not be fair to suggest voiding of the Options as a form of redress.

- Even though Mr D would have traded the Options in any case, available evidence is that he would not have opened as many positions as he did but for the margin calculation/application error.

- Gain should calculate the *surplus positions* that Mr D would not have been able to open if margin had been correctly calculated/applied for the Options and it should pay him the total loss he incurred on those positions. With regards to his claim for trouble and upset – for the misinformation and overall service deficiency from Gain that he is unhappy about – Gain's £2,000 offer is more than she would award Mr D, so she would not support an increase beyond that offer.

Gain calculated redress based on the investigator's approach; based on its identification of the specific trades (identified between the dates of 9 and 14 April 2020) that Mr D would not have been able to open if margin was correctly calculated/applied; and based, initially, on the end date of 22 April 2020 (when it says Mr D was definitely aware of the margin correction) but extended (on, it says, goodwill) to the date on which the Options expired. Its calculation has been shared with this service and it concludes with the total noted earlier in this decision.

The main difference between the parties is essentially that Mr D says he should be compensated for *all* the financial loss he incurred in *all* the Options from 21 April onwards, not just for the loss arising from the surplus positions that the investigator referred to and

that Gain identified. The investigator disagreed. She said he was obliged to mitigate his losses in the Options at the time he was told about the margin revision and had the opportunity to do so; that he ought reasonably to have done that by reducing his open positions in order to restore margin in the account and to regain access to trading in the account; but, instead, he refused to close any position, he kept them open throughout and they incurred further losses.

Mr D's lawyer says the investigator's approach was/is flawed; that the 24 hours notice he should have been, but was not, given is an important element she overlooked; that, with such notice prior to freezing his account, he would have placed hedging trades to address the margin breach and those trades would not necessarily have consumed more margin; that his loss resulted from being deprived the opportunity to mitigate by placing such trades; that it is unreasonable to expect him to have closed positions in the Options given the lack of clarity on how that was to be done, given the running losses within them and given that relevant legal authorities say he was not required to sacrifice his open positions in aid of mitigation; and that it would be unfair to penalise him for taking until 11 May to complete funding of the account, as that was dictated by his financial circumstances at the time.

The matter was referred to an ombudsman.

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.

Mr D's position on whether (or not) he would have traded the Options if margin was correctly calculated (and applied) is clear. As the investigator said, he has confirmed to us the background, planning and strategy behind the trades, and that they would have been placed at the time(s) they were placed in any case. However, as a preliminary observation during my review of the casefile, I did not consider that such clarity existed on whether (or not) he would have traded the Options with the same overall trade size if margin was correctly calculated and applied.

The investigator found that Mr D would not have traded the same overall size, because of evidence that he would not have had enough funds to do so. She found that he would have traded a lower overall size, hence her approach towards redress. My reading of the submissions in the case suggested to me that Mr D's earlier evidence appeared to support this finding, but he then appeared to say otherwise. The investigator shared my query about this with him and sought clarification, which he helpfully provided by confirming that, like the investigator found, he would not have had the funds to open the same overall size in the Options if margin had been correctly calculated and applied.

Certainty on the above two elements is important to determining this complaint. The first – that Mr D would have traded the Options irrespective of the margin calculation/application error – supports the investigator's finding that redress cannot reasonably be served by voiding or unwinding the Options. That type of redress would conflict with his position that the Options would have been traded in any case. The second element – that, had margin been correctly calculated and applied, his trading in the Options would have had a lower overall size – means that whilst the Options would have been traded even if the margin calculation error did not occur, the overall trade size would have been lower.

Thus far, the natural conclusion (from the above) is the redress proposed by the investigator, which I endorse and incorporate into this decision. Mr D is entitled to compensation for financial loss incurred from the surplus positions in the Options that he would not have traded – and would not have been able to trade – but for the margin calculation error.

Gain was initially reluctant to calculate this up to the date the Options expired. It considered that 22 April should be the calculation end point because it is by this date, at the latest, that the duty to mitigate passed to Mr D – but, as I said above, it extended its calculation to the Options' expiry date as a gesture of goodwill.

I understand this argument, and in another case (with supporting facts) it could be successful. In Mr D's case, and as I address further below, I agree that a duty to mitigate passed to him upon the notice he received on 21 April, and I accept that he held that responsibility in an overall sense from then onwards. However, the matter of the surplus positions is a precise one. Gain had to analyse and identify, with hindsight and full information, the specific trades that would and could not have been placed if the margin calculation error did not happen. If Gain had to do this in order to identify them, it stands to reason that Mr D would not have been able to identify them on 21 or 22 April – given that he was without such hindsight and without complete information. In this context, it would be unfair to say he had a duty to mitigate by closing – on 21 or 22 April or even thereafter – the specific trades (opened between 9 and 14 April) that Gain has now identified as the surplus positions.

It follows from the above that Gain has done the right thing by calculating redress for the surplus positions up to the date the Options expired. It is my finding that this is the correct basis on which to calculate compensation to Mr D for them. The next issue to address is the compensation he claims for the total financial loss he incurred in the Options between 21 April and 11 May. This claim includes the surplus positions, but as I have addressed those positions separately (above) I treat the claim as featuring only the overall trade size that Mr D would have placed but for the margin calculation error (that is, minus the surplus positions).

The key dispute in this claim is about *mitigation*. It is not disputed that Mr D had the duty to mitigate but there is disagreement about when this duty was triggered – given his argument that he remained without a proper explanation between 21 and 23 April – and about what this duty meant in real terms.

On balance, I find that Mr D had the duty to mitigate upon his receipt of the 21 April notification about the margin breach and about his options. The options he was given – to fund the account or reduce his open positions – related to lifting the account suspension, but they also lent themselves to his duty to mitigate.

His assertion about remaining uninformed, until 23 April, about the reason(s) for the margin breach is arguably irrelevant. On 21 April he was made aware of the margin breach, of his account being suspended (in terms of new trades, but not affecting the closure of existing open trades) and of the need to restore the level of margin required in the account (by either funding it or reducing the open positions within it) in order to lift the suspension. I do not suggest he was not entitled to also know the reasons behind the margin breach and I am mindful that he might have considered the entire affair to be a mistake that would be rectified. However, he was faced with the circumstances as they were on this date. He was responsible for addressing the margin breach, the account suspension and the open positions in the account. The fact that he queried the breach (and the reasons behind it) did not mean he could not have also addressed these responsibilities at the same time – and, in terms of mitigation, he ought reasonably to have done so.

In broad terms, mitigation is action that reduces the severity or seriousness of an event or occurrence. It is action, within reason, that is expected from and taken by the party facing the impact of the event or occurrence and it is arguably distinct from action challenging the relevant event, or occurrence, itself. It is for this reason that mitigation is generally viewed as

applicable even if a matter is to be subsequently disputed or is already under dispute. On balance, between 21 and 23 April Mr D should have coupled any enquires he pursued about the margin breach with effort to mitigate the impact of the account/trading suspension (and the open positions within the account).

Overall and on balance, I do not accept Mr D's lawyer's submissions on what mitigation meant – or was supposed to mean – for him; including the argument that the missing 24 hours notice and his inability to hedge diluted and/or altered his duty to mitigate. I repeat that Mr D was faced with the circumstances as they were on 21 April, and thereafter. He was not given the 24 hours notice that his lawyer has referred. I am satisfied that this is one of the elements behind Gain's offer to him of £2,000 for trouble and upset, and I address this further below. As far as mitigation is concerned, it remains a fact that the missing 24 hours notice and Mr D's inability to open hedging trades did not exhaust all mitigation options available to him at the time.

I am persuaded to conclude from Mr D's statements to this service that his priority at the time was not necessarily to mitigate. Instead, his priority appears to have been to continue the speculation for profit within his open positions. His statements to us repeated his reluctance to close the open positions at the time, including his assertion that decreasing the positions "… *would have meant unnecessarily and unfairly sacrificing about one third of all* [his] *account positions that* [he] *had worked hard to manage and enter at the best time and price*".

Mitigation required him to reduce the severity of the impact caused by the margin breach and/or account suspension. That could have been done by funding the account, but it is settled that he could not fund the account sufficiently in one step to restore margin and lift the suspension. He could only afford to fund the account in instalments over time. As such, there appears to be a loss of merit in his and his lawyer's arguments (or at least suggestions) that the inability to place hedging trades meant he was prevented from mitigating and that Gain unfairly sought to impose on him an invalid requirement to close positions. The reality of the situation was that funding the account and/or closing positions remained meaningful options available to him at the time, but the closure of positions became the only viable option because he could not afford to fund the account as required.

The point about placing hedging trades is inherently limited. No notice was given and the account was suspended in terms of new trades, so no hedging could take place. Was Gain wrong to deprive Mr D of notice? I consider that it was, and I accept that had such notice been applied before the account was suspended, he might indeed have pursued the hedging that he has referred to. Did that materially alter his duty to mitigate? I do not consider that it did. He could not hedge but he could have reduced the severity of the losses that began to accumulate by either closing positions to stem those losses or closing enough positions to restore margin in the account, lift the account suspension and then place any hedging trades (or any trades) he deemed necessary – and unlike the matter of closing the surplus positions, no specific identification was required in this respect, he could have closed any open positions.

By his account, closure of around a third of his open positions could (or would) have sufficed. The balance of available evidence suggests that he chose not to close those positions because he was hopeful that movement of the market would change in his favour and that all the positions would remain intact by the time he completed funding of the account and regained access to trading. This was speculation, not mitigation. It was aimed at keeping the positions open to pursue the prospect of profit and it was something he consciously did. A part of his lawyer's submissions to this service supports this finding and appears to affirm that his priority was indeed to speculate, not mitigate. His lawyer said the investigator was wrong to say he should have closed positions and that "… *had he done so*

he would have crystallised losses <u>when there was a possibility that the market would move in his favour</u>" [my emphasis].

In such circumstances, I do not consider that Mr D has a basis to say he discharged his duty to mitigate or a basis to claim compensation for loss incurred during a period in which he could have mitigated (and avoided or reduced the loss he has referred to), chose not to and chose instead to speculate. Gain cannot reasonably be responsible for the risk of loss from 21 April onwards that he wilfully undertook in order to speculate for profit.

For the sake of clarity, I do not criticise Mr D's overall pursuit of and speculation for profit in the Options. That was the obvious objective of his trading and he was entitled to seek that. I also do not say – and do not need to say – that speculation cannot ever coexist with mitigation. The point is that in Mr D's case the former featured whilst the latter appears to have been non-existent. The matter I am addressing is whether (or not) he discharged his duty to mitigate, so it would not be fair to find that there was mitigation on his part where little to none appears to have happened. It is noteworthy that, as his lawyer stated, the account held around £97,000 in value on 21 April which dropped to around £7,600 on 11 May (after his additional funding of over £20,000 into the account during this period), so the implication is that this amount – or an amount around this level – could potentially have been saved had Mr D mitigated and closed positions on 21 April. Perhaps even more could have been saved given that most or all the additional funding he made during the period would probably have been unnecessary – in terms of lifting the suspension – if positions were closed on 21 April.

The account suspension, in isolation, was not a wrongdoing. The idea of preventing Mr D from opening new trades when a margin breach already exists – and is yet to be repaired – stood to assist him in mitigation. That is, it stood to avoid the risk of new trades creating new losses and new pressure on margin.

I do not accept the suggestion that the notion of closing positions required additional clarity. Mr D's lawyer says the notice on 21 April did not specify how this was to be done. The notice referred to the option of reducing open positions and, on balance, I consider that this was self-explanatory in terms of meaning the closure of open positions.

I have considered the legal authorities, on mitigation, his lawyer referred to. The thrust of the argument is that Mr D was not required to close his positions and that, in the circumstances of his case, it was not unreasonable for him not to have done so. Overall and on balance, I do not consider that the legal authorities that have been cited defeat the analysis I have set out above or justify Mr D allowing substantial total losses – up to the level of £111,000 that he claims – to accumulate in open positions over the course of around three weeks when he could have avoided all, most or a significant part of such losses (for his own benefit) had he closed positions at the outset.

This was not a matter of the closure of positions being unjustly imposed upon him, it was a matter of such closures being in his best interest to avoid the accumulation of losses he could not hedge or trade against whilst the account was suspended. If he argues that he would not have been in the position he found himself if Gain's initial margin calculation error had not happened and that he was entitled to pursue the profit he had planned for by trading the Options, nothing prevented him from mitigating his losses as a priority (again, for his own benefit) and then considering, perhaps with advice, a pursuit for lost opportunity to make profit. He did not do this, instead he appears to have taken the opportunity to make profit at the expense of mitigation but unfortunately for him that opportunity did not yield profit. Had it yielded profit he would not have met the total loss that he met when he regained full control of the account on 11 May, and he would have had no such loss to complain about. None of these seek to criticise Mr D. He was entitled to make his own decisions in the matter, but the decisions he made and steps he took mean that Gain cannot fairly be held responsible for

the loss that he claims.

Putting things right

To compensate Mr D fairly, Gain must pay him the total loss he incurred in the surplus positions from when they were opened to when the Options expired – as I addressed above. Gain has identified the specific surplus positions and it has calculated this compensation. It appears that the calculation has been shared with Mr D, if this is not the case I order Gain to share the calculation with Mr D without delay. I order Gain to pay Mr D the total compensation amount in this respect plus interest on the compensation amount at the rate of 8% simple per year from when the total loss was crystalised – when the Options expired – to the date of settlement. This is to compensate Mr D for being deprived of the compensation amount during this period.

Gain was wrong in its failure to give Mr D the 24 hours notice he was entitled to. It also appears that it was not completely clear with him about the reason(s) behind the margin breach on 21 April when margin for his account was revised and when new trading in his account was suspended. I also note his displeasure about the misleading information he refers to before he says the situation became clear on 23 April. For all these matters, the implication of poor service within them and the service level impact they caused to Mr D, I agree that he should be compensated for the trouble and upset he faced. Gain has offered him £2,000 and, like the investigator, this amount is more than I would order in the circumstances of his case. As such, I do not order Gain to pay him any more than this for trouble and upset, but I conclude his claim for trouble and upset compensation on the understanding that it is a claim settled by the £2,000 Gain has offered and will be paying him.

My final decision

For the reasons given above, I uphold Mr D's complaint and I order Gain Capital UK Limited to resolve compensation to him as I have set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr D to accept or reject my decision before 1 June 2022.

Roy Kuku
Ombudsman