

## The complaint

Mr T complains that Tier One Capital Ltd ('TOC') gave him unsuitable advice when they recommended him multiple times to invest in the West Auckland (WA) Project, a private funding circle (PFC) investment.

Mr T invested both from personal funds and later through his Self-Invested Personal Pension (SIPP). His SIPP investment forms part of a separate complaint, so this decision only deals with Mr T's personal investment which he made with funds previously held on a deposit account.

## What happened

Mr T was advised in April 2015 to invest £25,000 into the WA project. It was a lending project which started in 2015 to provide funding for a development of 110 houses. The investment was part of a syndicated property loan with a term of two years. The funds in April were planned to be used to support the purchase of some land, the acquisition of planning permission and to carry out pre-liminary works ahead of a full site development. Initial interest of 10% per year was to be paid to investors quarterly.

In December 2015 and February 2018 he was again advised to invest £25,000 each time for the next stages of the WA project.

TOC says interest payments stopped in late 2019 when the project suffered financial difficulties. From what I understand there is no concrete prospect of when or if capital repayments or further interest payments will be paid. TOC said eventual losses would be known by the end of 2021, but the Financial Ombudsman Service has not been informed by either party that any further pay-outs have happened.

Mr T complained in 2020. He says the investment has not carried the security in assets that was promised. He says he was a cautious investor and he was not interested in risk believing the investment to be asset backed. In an email to TOC in June 2020 he said:

*These investments were sold to me on the basis there was very little to no risk as the security would always cover any shortfall.*

TOC admitted in their initial response to Mr T in May 2020 that there had been gaps in their sales advice process and record keeping and they said there were inconsistencies in the information Mr T was provided with. The adviser who had recommended the WA investment to Mr T was not working for TOC anymore. They said it was unclear whether the advice to invest into WA had been suitable or not.

They offered Mr T to delay the complaint resolution until the outcome of the project and full losses would be known. TOC said they would then revisit the complaint. Alternatively, they offered to use a forecasted capital loss position of 40%. After deducting interest payments Mr T already received on his total direct investment into WA (which included £100,000 invested through his SIPP), they calculated losses to be £10,000 and offered to pay another £1,000 to acknowledge they had fallen below their service standards. They offered to keep

this sum in TOC's account accruing interest of 3% a year and use it to pay for ongoing charges or-if Mr T didn't want to use their services anymore-pay the sum of £11,000 to him directly.

Mr T rejected the proposals and referred his complaint to this service. TOC provided their file to the Financial Ombudsman Service. At this point they said the advice given was suitable. Our investigator upheld the complaint in part. TOC had categorised the first funding tranche in 2015 as a low to moderate risk investment, the second one in December 2015 as moderate risk and the one in February 2018 as high risk. The investigator considered Mr T was a cautious investor and that the WA investment exceeded his attitude to risk. However, due to Mr T's substantial holdings in cash, he felt the relatively small investment amount of £25,000 wasn't excessive and could be tolerated.

However, he felt Mr T shouldn't have been advised to invest again in December 2015 and February 2018 as his exposure to PFC by this point had increased. The investigator assumed that Mr T was investing additional sums of £25,000 each time, i.e. £75,000 in total. In response TOC pointed out that the first two loans were redeemed and capital returned. So whilst he was advised three times to invest £25,000, the capital was essentially recycled, so Mr T only directly invested £25,000 into WA outside his SIPP. As the investigator had concluded the first investment of £25,000 was suitable, TOC felt this complaint should not be upheld.

As no agreement could be reached, the complaint was referred for an ombudsman's decision.

### **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.

I've previously issued a provisional decision and gave both parties further opportunity to comment. In my decision I said the following:

TOC gave Mr T investment advice and so they needed to make sure their recommendations were suitable for him.

Mr T met with TOC in 2015. A meeting note dated 3 February said:

*[Mr T] explained he would ideally wish to simply generate an income a bit better than what he currently is achieving with a raft of cash deposits with the mainstream banks. [TOC] discussed the importance of completing the risk questionnaire to allow a more informed decision on where best to allocate funds within risk parameters they will be comfortable with and which achieve their goals.*

Mr T and his wife completed a risk questionnaire which showed Mrs T was very risk averse. Mr T was recorded as being risk category 4 which I assume was equivalent to lowest medium risk. He said on his attitude to risk form he was neither risk averse or a risk taker. He strongly agreed or agreed with statements which said:

- *I have been extremely cautious in my past financial investments.*
- *I believe that it is reckless to take financial risks*
- *When I'm faced with a financial decision I am generally more concerned about the possible losses than the possible gains*
- *I would rather get a guaranteed rate of return than be uncertain about my investments.*

- *I do not feel comfortable with financial uncertainty.*

And he disagreed with:

- *I would accept potential losses in order to pursue long-term investment growth*
- *Taking investment risks is important to me*

He ticked a box to say he felt *slightly comfortable* when he took a financial risk and small/medium losses could be tolerated.

Having looked at the questions he answered I agree with the investigator that he was a cautious investor. This is also backed up by the fact that Mr T and his wife held the majority of their money in cash and premium bonds in 2015. Mr T also had a pension and company shares. And another meeting note on 4 February 2015 said the adviser explained the risk questionnaire suggested Mr T had a preference for lower risk investments.

From what I've seen Mr T wanted to get better returns than he got from cash deposits. However, I don't think the evidence suggests he needed or wanted to take much risk with his money.

I appreciate Mr T was high net value client with large sums of cash available to invest. And in comparison to his assets the sum invested was relatively small. So I agree that he had the financial capacity to lose some of his investment. However, I don't think the PFC investments matched his attitude to risk and were generally suitable for him.

He didn't have any significant investment experience and so I'm not persuaded he would have had the relevant knowledge and experience to fully understand the risks these investments held. These were unregulated investments with substantial liquidity and market risks. The project was also in its early stages with no obvious track record.

Mr T kept referring to these investments being 'asset backed' and a couple of years later he said he preferred 'bricks and mortar' to equity investments. TOC seems to take this as evidence that Mr T understood what he was doing, however I take a different view.

I think Mr T likely thought the idea of having land or properties acting as a security was reassuring and he might have felt he understood the concept of investing in property better than equities which he didn't have experience with and might have felt more abstract and volatile to him. Also TOC told him this was a low to moderate investment which would have given him no reason to think otherwise.

But as I said above, I'd say this investment from the start was a higher risk, non-standard and unregulated investment. I don't think Mr T would have understood the full risks of the PFC proposition in general. His wife was risk averse and he was cautious. I don't think the PFC investments were right for them.

They had no need to take risk with their money to achieve high returns. Their financial situation in my view was comfortable and a diversified low risk portfolio of standard investments which could have included for example bonds, gilts and property funds (if Mr T didn't want to invest much in other equity shares) would have been far more suitable in my view.

Whilst TOC have said the first investment was a low to moderate investment, I disagree. It might have been less risky than later funding tranches, but I still think this non-standard investment was a lot higher risk than Mr T was willing to take.

Overall, I don't think the WA investment should have been recommended to Mr T in April 2015 or subsequently in December 2015 and February 2018.

### *Responses to my provisional decision*

TOC disagreed with my decision. I'm not going to repeat everything they said, but their key arguments are:

- Since Mr T made his complaint in March 2020, capital repayments totalling £10,750 have been made and a final payment of £1,500 was anticipated by the end of April 2022 which would bring the project to a close. In addition he has received £10,347.62 in interest. Once the project is concluded in April, Mr T's investment will have returned £22,597.62, so Mr T has lost £2,402.38 of his original £25,000 investment. TOC says this is the actual loss and is insignificant relative to Mr T's asset base. This also falls within his capacity for loss.
- The investments sat within Mr T's risk tolerances. Mr T was a cautious investor with a risk level of 4 out of 10, defined by a potential fluctuation in value of 20%. This doesn't mean he wasn't prepared to take any risk and Mr T had confirmed small/medium risks could be tolerate and he was slightly comfortable when taking financial risk.
- Toc doesn't understand why I referred back to information from 2015 when the complaint is about the investment in 2018. At the time investments were made in 2018 Mr and Mrs T had £460,000 in cash and premium bonds, £253,000 invested with TOC, £200,000 invested in private company shares (including £100,000 invested in a new start up business supporting property development), £110,000 in a buy to let property and £202,000 in cars. It's misleading to say the vast majority of their assets were in cash and premium bonds.
- Mr T did know what he was doing. He was an experienced and accomplished investor who has regularly invested into small private companies and speculative property developments (both before the WA investment and after) without TOC's advice.
- Mr T was provided with clear, complete and detailed information outlining all the risk of the investment which he is familiar with given he has a number of these investments. He signed documents to say he fully read and understood them and he was recommended to seek independent legal advice before proceeding with any investment.
- As a business and investment property owner he regularly enters into legal documentation and has invested multiple times into small, private start-up businesses to benefit from HMRC approved tax reliefs (such as EIS and SEIS), has built a multi-million pound asset base through business and is a frequent investor into a variety of different investment vehicles. Mr T has robust business and investment knowledge.
- Mr T was one of the original angel equity funders of a new banking entity focused on providing development finance to the property sector. This investment was made externally to Tier One Capital and provides further evidence that Mr T has a good understanding of investing into projects that are exposed to the property development sector. This investment was made before Mr T decided to invest into

the WA investment and he has continued to invest equity into this venture over the past few years.

- Mr T has told TOC he continues to have an advisory relationship with TOC's previous adviser who gave him the WA advice and has since left TOC. He continues to invest in illiquid and high-risk products.
- Mr T has enjoyed an overall positive return on his portfolio, which must be taken into account as part of this complaint. Mr T fully understood and continues to understand all investment decisions he made and continues to make.

I've carefully re-considered TOC's submissions during this complaint as well as their latest submissions, however I remain satisfied that the investment into WA shouldn't have been recommended to Mr T.

Mr T complained about all his WA investment, so I've considered both the 2015 investments and the one in 2018 (outside the SIPP) in this complaint. I disagreed with the investigator that the first investment in 2015 was suitable for the reasons outlined in my provisional decision which is set out above.

I acknowledge the couple had some capacity for loss and I didn't say Mr T wasn't prepared to take any risk. I also can see that Mr T was a high net worth individual. However, the WA investment, which was unregulated, was in my view too high risk. And based on his recorded circumstances at the time I can't see he had the required knowledge and investment experience to fully understand the risks of this investment. I remain of the view the WA investment should not have recommended to Mr T in 2015. And I see no reason why Mr T would not have followed TOC's recommendation not to invest.

Mr T made his second investment six months later when the first one had completed and he simply reinvested his capital of £25,000. If he had not been advised to invest in April 2015 into WA, he would not have been in a position where his capital was returned and be recommended to invest it in the second stage of the project. I think on balance this second and third investment into WA would not have happened.

However, even if I consider that after not investing in WA in 2015, he somehow would have sought advice again in 2018, I think the investment wasn't suitable then either. I do acknowledge that by 2018 Mr T had a portfolio of TOC investments. However, he had invested based on advice he received from TOC, so I don't think his knowledge and understanding of risks automatically would have increased. From what I've seen he trusted the adviser to recommend investments which were in line with his attitude to risk. The fact that he did already had a portfolio of TOC direct lending investments by that point means further investment would have exposed him to even more risk.

Mr T has business experience and seems to be interested in property investments. However, based on the evidence provided I still think the WA investment was not suitable for him and shouldn't have been recommended.

I also don't think the fact that by 2018 he had a buy-to let property or private company shares changes the fact that the WA investment was too high risk.

The fact an investment was successful or that future investments possibly didn't lose Mr T a large amount of money does not mean these investments were suitable.

Also providing Mr T with information material or risk warnings does not make an unsuitable investment suitable. I also note that in 2018, when TOC said WA was a high-risk investment, they reassured Mr T in their suitability report that

*'the project is asset backed to a strong degree, and whilst this remains a private loan supporting a single project the project carry's a relatively conservative loan to Gross Development Value. The process outlined is therefore one which we feel can mitigate a large portion of the risks inherent in this activity however it is still sensible for each investor to acknowledge the potential for such a project to change in shape or form as the project progresses.'*

I don't think this made it clear enough how much risk this investment really entailed and how this differed from the investments recommended before in the same project which were previously described as low and moderate investments.

In my view this investment from the start was a higher risk, non-standard and unregulated investment. Although I appreciate risk factors were described in the suitability report, I don't think Mr T would have understood the full risks of the PFC proposition in general. And as explained previously the fact find and suitability report do not suggest Mr T wanted to take much risk with his investments.

Of course risk attitudes can change and it's possible Mr T has been investing in higher risk investments since. However, based on his risk questionnaire in 2015 (which TOC has confirmed wasn't updated in 2018) and his circumstances in 2015 and 2018, I don't think the WA investment was suitable.

Mr T has specifically complained about his WA investment and that he was exposed to it multiple times through personal investment, through his pension and through shares (which is a separate complaint). I appreciate Mr T might have not raised a complaint about other TOC investments which were more successful. But I would only expect him to raise a complaint about advice he was unhappy with. There is no doubt the underperformance and liquidity issues triggered Mr T's complaint about WA. And he is entitled to complain. If the advice given by TOC had been suitable this complaint would not be upheld. So I don't think it's unfair or unreasonable to look at Mr T's specific complaint here.

I think it's fair however that Mr T's gains and interest payments from his £25,000 investment in April and December 2015 are taken into account when calculating redress as they are linked and my award allows for this.

### **Putting things right**

In assessing what would be fair compensation, I consider that my aim should be to put Mr T as close to the position he would probably now be in if he had not been given unsuitable advice. With suitable advice I think Mr T would have invested £25,000 differently in April 2015 and would not have invested this sum again in December 2015 and February 2018. I don't know exactly where Mr T would have invested his money instead, however I think the below recommendation is fair and reasonable in the circumstances.

### **What should TOC do?**

As I understand it Mr T's first and second investments in 2015 were both successful and he received interest payments. It is the investment in February 2018 which is in difficulty and which might cause Mr T losses.

Both Mr T's gains and losses from the WA investments need to be taken into account here,

as with suitable advice he also wouldn't have earned any interest from the WA investments. To compensate Mr T fairly, TOC must:

- Compare the value of Mr T's outstanding WA investment with that of the benchmark shown below and pay the difference between the *fair value* and the *actual value* of the investment. If the *actual value* is greater than the *fair value*, no compensation is payable. Mr T's first and second investment paid interest and the loans were redeemed.
- TOC should also pay interest as set out below.

Income tax may be payable on any interest awarded.

investment name	status	benchmark	from ("start date")	to ("end date")	additional interest
WA investment	Still exists but illiquid	For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds	April 2015	Date of my final decision	8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance)

### **Actual value**

This means the actual amount payable from the investment at the end date.

If at the end date the investment is illiquid or like in this case it's uncertain how much capital and/or interest will be returned, it may be difficult to work out what the *actual value* is. In such a case the *actual value* should be assumed to be zero. This is provided Mr T agrees to TOC taking ownership of the investment, if it wishes to. If it is not possible for TOC to take ownership, then it may request an undertaking from Mr T that he repays to TOC any amount he may receive from the investment in future.

I appreciate TOC wanted to wait until the value of the investment is known. And given some time has passed since my provisional decision, this might be the case now. However, even if the value isn't known yet, I don't think it's fair for Mr T to have continued uncertainty, so calculations should be done now.

### **Fair value**

This is what the investment would have been worth at the end date had it produced a return using the benchmark.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, TOC should use the monthly average rate for one-year fixed-rate bonds as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

Any withdrawal, income or other distributions paid out of the investments should be deducted from the fair value calculation at the point it was actually paid so it ceases to

accrue any return in the calculation from that point on. If there is a large number of regular payments, to keep calculations simpler, I'll accept if TOC totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically. If any distributions or income were automatically paid out into a portfolio and left uninvested, they must be deducted at the end to determine the fair value, and not periodically.

### **Why is this remedy suitable?**

I have chosen this method of compensation because:

- Mr T wanted Capital growth with a small risk to his capital.
- The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to his capital.
- The FTSE UK Private Investors Income total return index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds. It would be a fair measure for someone who was prepared to take some risk to get a higher return.
- I consider that Mr T's risk profile was in between, in the sense that he was prepared to take a small level of risk to attain his investment objectives. So, the 50/50 combination would reasonably put Mr T into that position. It does not mean that Mr T would have invested 50% of his money in a fixed rate bond and 50% in some kind of index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of return Mr T could have obtained from investments suited to his objective and risk attitude.

### **My final decision**

I uphold Mr T's complaint and require Tier One Capital Ltd to calculate and pay compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr T to accept or reject my decision before 9 August 2022.

Nina Walter  
**Ombudsman**