DRN-3553944

The complaint

Mr M has complained to Kession Capital Limited ("Kession") about information and advice he says he was given by one of its appointed representatives ("AR") – Swan Securities & Investments Limited ("Swan").

What happened

In October 2015 Mr M made a £5,000 investment in an opportunity called 'Sooner Energy' which invested in oil in America. He says he had been contacted by Swan who advised him and arranged the investment.

Mr M complained that he was assured by the Swan adviser that the investment was part of a long programme which would pay dividend returns that would likely increase in the future from around 5% to 12%. However, he says the information and advice he was given was wrong as the dividend payments were irregular and much lower than expected – until they eventually stopped.

A complaint was made to Kession and Mr M says it's responsible because Swan was its AR and was operating under its umbrella at the time.

Kession didn't uphold Mr M's complaint. In summary it said that although Swan was its AR at the relevant time, it isn't responsible for the acts complained about because Swan acted outside of what it was allowed to do under its agreement with Kession.

In particular, Kession said Swan was not entitled to approve its own financial promotions and had agreed to seek approval from Kession in advance for all financial promotions by whatever means prior to use. Furthermore, it never signed off on any financial promotion regarding Sooner Energy.

So, whilst Kession acknowledged the investment was marketed and sold by Swan, it says it was done outside of the AR agreement and so could not comment on whether advice was given, or the investment was mis-sold.

Mr M disagreed with Kession and referred his complaint to this Service. He says Kession had a duty of care to monitor what Swan was doing, and also says before making the investment he had contacted the Financial Conduct Authority ("FCA") to put his mind at rest that he was dealing with a regulated business.

I issued a provisional decision in early April 2022. In that decision I concluded that Kession was responsible for Mr M's complaint and that it should compensate him. I've included a large extract of my provisional decision below.

> ***Jurisdiction***
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> …I cannot decide jurisdiction based upon what I consider to be fair and reasonable in all the circumstances. That is the basis on which the merits of complaint will be determined if we have jurisdiction to consider it.

The Financial Ombudsman Service can deal with certain complaints against Kession as a regulated firm/authorised person. That may include complaints about the acts or omissions of its ARs. That is why this complaint is made against Kession rather than Swan.

We are governed by the DISP rules which are set out in the Financial Conduct Authority's ("FCA") Handbook. They contain the factors that need to be considered when looking at the compulsory jurisdiction of this Service.

We can consider a complaint if it relates to an act or omission by a firm in carrying out one or more of the listed activities, (including regulated activities), or any ancillary activities carried on by the firm in connection with those activities (DISP 2.3.1R).

Complaints about acts or omissions by a firm include complaints about acts or omissions in respect of the activities for which the firm is responsible (including the business of any AR for which the firm has accepted responsibility), (DISP 2.3.3G).

I think it's useful for me to explain what the terms 'appointed representative' (AR) and 'Principal' mean. The Financial Services and Markets Act 2001 ("FSMA"), states that the general position is that if a person carries on a regulated activity and they are not an authorised person – they will be committing a breach of law under s.19 and s.23 FSMA). But there is an exemption to this for an AR.

An AR is essentially a firm or person who conducts regulated activities but does so under the umbrella of a firm the FCA directly authorises (the Principal). The AR itself doesn't need to have authorisation from the FCA to conduct regulated activities. The exemption is set out in s.39 FSMA:

"39. Exemption of appointed representatives.

(1) If a person (other than an authorised person) –

(a) is a party to a contract with an authorised person ("his principal") which –

(i) permits or requires him to carry on business of a prescribed description, and
(ii) complies with such requirements as may be prescribed, and

(b) is someone for whose activities in carrying on <u>the whole or part of</u> that business his principal has accepted responsibility in writing'

he is exempt from the general prohibition in relation to any regulated activity comprised in the carrying on of that business for which the principal has accepted responsibility.

…

(3) The principal of an appointed representative is responsible, to the same extent as if he had expressly permitted it, for anything done or omitted by the representative in carrying on the business for which he had accepted responsibility." (my emphasis).

So, under s.39 the principal is required to accept responsibility for the business being conducted by the AR. And the case of *Anderson v Sense Network* [2018] EWHC

2834 makes it clear the words *"part of"* in s.39 allow a principal firm to accept responsibility for only part of the "*business"* conducted by an appointed representative.

Kession's position:

Kession has made a number of points in response to the complaint and in relation to jurisdiction. In short it says it did not, and does not, accept responsibility for the acts about which Mr M complains and the ombudsman service does not have jurisdiction to look at a complaint against it.

So, I think there are three important points to consider when looking at our jurisdiction to consider this complaint against Kession:

(a) what are the acts about which Mr M has complained?

(b) were those acts done in the carrying on of a regulated activity or an ancillary activity carried on in connection with a regulated activity (DISP 2.3.1)?

(c) were they acts for which Kession accepted responsibility (s.39(3) FSMA)?

What are the acts about which Mr M has complained?

In order to decide whether we can or cannot consider a complaint, it's necessary to decide what Mr M's complaint is.

Mr M says that he was given incorrect information and unsuitable advice to make an investment in Sooner Energy. Kession states it cannot comment on whether advice was given but has acknowledged Swan marketed and sold the investment.

The difference between providing information and giving advice can be a fine line. I can't be sure whether or not Swan gave advice to Mr M, but the available evidence does make it clear that Swan promoted the investment in Sooner Energy.

So, whilst Mr M says his complaint is about the information and advice he was given by Swan, it's clearly about Swan's involvement in the transaction overall. So, in my view the acts which Mr M's complaint relates to, are the promotion and arrangement of the investment and Sooner Energy.

Were those acts done in the carrying on of a regulated activity or an ancillary activity carried on in connection with a regulated activity (DISP 2.3.1)?

As I've said above, we only have jurisdiction to look at regulated activities (DISP 2.3.1).

Section 22 FSMA defines "regulated activities" as follows:

"(1) An activity is a regulated activity for the purposes of this Act if it is an activity of a specified kind which is carried on by way of business and

(a) relates to an investment of a specified kind;…

(4) "Investment" includes any asset, right or interest.

(5) "Specified" means specified in an order made by the Treasury."

The relevant Order is the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO). Article 4 provides:

"4. – Specified activities: general

(1) The following provisions of this Part specify kinds of activity for the purposes of section 22(1) of the Act (and accordingly any activity of one of those kinds, which is carried on by way of business and relates to an investment of a kind specified by any provision of Part III and applicable to that activity, is regulated activity for the purposes of the Act)."

Arranging deals in investments is a specified activity (Article 25). And so is agreeing to advise on investments or arrange deals in investments (Article 64).

Acts such as obtaining and assisting in the completion of an application form and sending it off, with the client's payment, to the investment issuer would come within the scope of Article 25(1), when the arrangements have the direct effect of bringing about the transaction. I am satisfied the arranging Swan carried out here falls within the scope of Article 25(1). Given the close connection, I am also satisfied the promotions were ancillary to the arranging.

So, I'm satisfied the acts complained about were done in the carrying on of a regulated activity.

Were they acts for which Kession accepted responsibility?

Mr M has directed his complaint to Kession, and the AR agreement was in place at the relevant time, so I'm satisfied Swan was an AR of Kession.

Whether Kession is responsible for the specific acts complained about is determined by considering the terms of the contract between it and Swan. Some terms of an AR agreement work to exclude liability for a Principal, and some do not.

I've carefully considered the entirety of the AR agreement and I'm satisfied that the acts which Mr M's complaint relate to are ones which Kession accepted responsibility for.

It's not the case that a principal is not responsible for business in *any* instance where *any* term in an appointed representative agreement is not adhered to. The High Court judgment in the case of Anderson v Sense Network (2018) makes it clear section 39 FSMA allows a principal firm to accept responsibility for only part of the generic "business of a prescribed description". In other words, Kession was entitled to appoint Swan as a representative and limit the scope of the regulated activities it could carry out and that it would be responsible for.

But the Court of Appeal judgment in the same case set out that only restrictions on "*what*" generic business could be conducted would limit the principal's responsibility. In contrast, restrictions on "*how*" that business is to be conducted don't limit a principal's responsibility. In other words, a principal (Kession) can't avoid responsibility for activities it authorised an AR (Swan) to carry out just because those activities weren't carried out in the way it wanted them to be.

Having considered the AR agreement between Kession and Swan, I think some of the terms relate to *how* Swan was to carry out the business which Kession accepted responsibility for, rather that *what* business Swan could carry out.

At 6.1 the contract says:

The Appointor hereby accepts responsibility for all the AR's and the Individuals' activities in carrying on the Relevant Business under this Agreement.

Relevant Business is defined as:

Regulated activities which the AR is permitted to carry out under this Agreement which are subject to the limitations of the Appointor's part IV permission as detailed in Schedule 5. For the avoidance of doubt, the AR is not permitted to carry out any investment management activities. The AR is permitted to market and promote its services, arrange business and give advice. The AR will conduct business with professional clients, elective professional clients and eligible counterparties. In circumstances where clients do not satisfy the criteria to opt-up to elective professional status, the AR may treat them as retail clients and conduct business with them as such insofar as it is restricted to promoting and arranging only. The AR is not permitted to give advice to retail clients. When conducting with retail clients the AR will at all times adhere to the strict guidelines outlined in Schedule 6. The Appointor acknowledges that the AR will conduct capital raising and arranging activities via the issuance of corporate bonds for power projects. There is no pooling of capital and no CIS.

This accepts the AR will conduct capital raising and arranging activities via the issuance of corporate bonds for power projects and notably says this without qualification or restriction. So, Kession's part IV permission (as detailed in Schedule 5) includes arranging of investments of the type made by Mr M. Accordingly, under 6.1 the starting point is that Kession accepts responsibility for it.

At 1.3 the agreement gives Kession the right to impose restrictions as follows:

In accordance with section 39 of FSMA and the FCA Handbook, the Appointor may impose restrictions:

a) on the AR preventing the AR from procuring or attempting to procure persons to enter into investment agreements;

b) as to the types of investment and investment activity in relation to which the AR may act, even if those activities and/or investments form part of the Relevant Business…

So, it's clear that the agreement did allow Kession to put restrictions in place which may have related to *what* Swan could do (rather than just *how* it could do it). Having considered what restrictions in the agreement are relevant in this complaint, I've seen nothing to show Kession put any restrictions on arranging investments.

2.2 of the agreement states:

The AR shall not make any financial promotion (including but not limited to unsolicited real-time financial promotions) unless such promotion relates to Relevant Business and is either approved in advance by the Appointor or is made only within circumstances where an exemption applies under the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 as amended from time to time.

And 2.3 of the agreement states:

The AR acknowledges that it is not entitled to approve financial promotions for the purposes of section 21 of FSMA and undertakes that it shall not do so, or purport to do so.

These restrictions only relate to promotion and do not place any restrictions on arranging. 2.2 is not a restriction on the Relevant Business, is it, as it refers only to financial promotion which isn't, in itself, a regulated activity. It doesn't put any restrictions on arranging or advising.

Although 2.3 relates to an activity which requires regulatory authorisation, it also does nothing to restrict advising or arranging.

So even if promotion in itself wasn't permitted and the AR wasn't permitted to approve itself, the arranging and advice clearly fall within the Relevant Business and the promotion activities are connected to them. Kession accepted responsibility for the arranging of investments, and in my view the promotion of investment (even if carried out in breach of the AR agreement) which was 'inherently bound up' with the arrangement – and so is something Kession is also responsible for. This approach was set out by the courts in Martin & Anor. v Britannia Life Ltd [1999] and Tenetconnect Services Ltd, R (on the application of) v Financial Services Ltd & Anor [2018].

Given that I'm satisfied Kession accepted responsibility of the acts complained about, I have gone on to consider what is fair and reasonable in the circumstances of Mr M's complaint.

What is fair and reasonable in the circumstances of Mr M's complaint

Mr M is unhappy as he says he was assured by Swan that the investment would generate dividend payments starting at around 5% and rising to 12% - but that level of return was never achieved and ultimately the funds Mr M invested have been lost. So essentially Mr M has said Swan made representations that were incorrect and misleading.

COBS 4.2 requires a firm to make sure that any financial promotion is fair, clear and not misleading. In this case I can't reasonably say that it was.

The promotion of the Sooner Energy investment to retail clients such as Mr M was subject to restrictions and Swan, acting on behalf of Kession, had to meet regulatory obligations which included treating customers fairly and acting in their best interests.

Those regulatory obligations set out in the FCA's Principles for Businesses (of which I think Principle 6 "*Customers' interests – A firm must pay due regard to the interest of its customers and treat them fairly*" is the most relevant here) and in COBS 2.1.1R ("*A firm must act honestly, fairly and professionally in accordance with the best interests of its client*.").

The rules on financial promotions at the time (set out in COBS 4) said promotion of investment of the type made by Mr M to retail clients was restricted to investors which fell within certain categories such as "high net worth", "sophisticated" and "restricted". These categories were defined and a process for placing an investor into them set out.

I have not seen sufficient evidence to show Swan took the necessary steps to check if Mr M fell into one of the categories (and it follows it also did not take the necessary steps for putting him into a category). And from the information I have about Mr M I also think it unlikely he could have been put into one of these categories, had the necessary steps been taken. So had Swan acted fairly and reasonably to meet the relevant rules, it would have been aware Mr M was not eligible to receive promotion for the investment.

The alternative basis on which the investments could have been promoted to Mr M was if he were a professional client. However, I've seen no evidence to show any efforts were made by Swan to see if Mr M could be treated as a professional client, or to follow the process set out in the rules for this.

I think acting fairly and reasonably to meet its regulatory obligations, Swan should not have proceeded to make the promotion and arrange the investments in such circumstances. Were it not for the actions and misrepresentations of Swan, I think it's unlikely he would have made the investment in Sooner Energy at all. So, I think it's fair to ask Kession to compensate Mr M for the loss he has suffered.

Responses to my provisional decision

Mr M accepted my provisional decision and had nothing material to add.

Kession disagreed with my findings. In summary, it responded saying it should not be held responsible for a product that wasn't approved by it. This was accompanied by evidence submitted from a similar complaint involving Swan and the same investments – which it suggests demonstrates Swan was acting in a way that deliberately concealed its activities.

Kession also quoted a section of its AR agreement with Swan which it says makes it clear that Swan (as an AR) had no ability to market a product that had not received prior approval:

"1.5 This Agreement shall terminate automatically in the event of:

…

e) the AR promoting any product or service, that falls within the jurisdiction of the FCA rules, that has not been approved by the Appointer prior to its release;

f) the AR failing to put in place adequate professional indemnity insurance prior to carrying out any regulated business."

So, in reaching a final decision on Mr M's complaint, I've reviewed matters again including the additional points made by Kession.

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 considered everything, I remain of the same overall conclusions as set out in my provisional decision.

I've first reviewed the further points Kession has raised in relation to jurisdiction. I don't have the discretion to decide what is fair and reasonable in relation to this point – but must apply the rules as they apply. I explained my thoughts on whether Kession is responsible for what

Mr M complains about in my provisional decision and set that out above – so won't repeat everything again here.

In summary, even if the promotion of an investment in itself wasn't permitted by Kession and the AR wasn't permitted to approve itself, the arranging and advice clearly fall within the Relevant Business and the promotion activities are connected to them. Kession accepted responsibility for the arranging of investments, and in my view the promotion of investment (even if carried out in breach of the AR agreement) which was 'inherently bound up' with the arrangement – and so is something Kession is also responsible for.

I've reviewed the clause specifically referred to by Kession in response to my provisional decision – but I'm not persuaded that changes the position. I acknowledge that it does demonstrate an intent on the part of Kession to not accept responsibility for business without specifically approving its promotion. But as I've already explained – the agreement with Swan did accept responsibility for arranging and advice – which is what makes Kession responsible.

Also, I note clause 1.5 relates to what would trigger the automatic termination of the agreement between Swan and Kession. So, the context doesn't relate to whether Kession accepted responsibility for the business, but rather what would happen if Swan proceeded to promote investments without prior approval. Kession has suggested that Swan was promoting and arranging business for which it wasn't seeking approval for some time – but the agreement continued to operate in any event. I recognise that Kession may say that it did not know about the acts of Swan at the time, but nevertheless I've seen nothing to suggest the agreement wasn't in place at the time of Mr M's business being placed.

Whilst I do understand Kession's frustration, I maintain that for the reasons detailed in my provisional decision and set out above, it is responsible for Swan's acts in relation to Mr M's complaint.

Having decided that Kession is responsible for Mr M's complaint I remain of the view that he should be compensated for the actions and failures of Swan. Essentially Swan made representations to Mr M which were incorrect and misleading – as the levels of risk and likely returns were misrepresented.

The obligations Swan had when dealing with Mr M were explained in my provisional decision and are set out above. In summary, it had an obligation to comply with Principle 6 of PRIN ("*Customers' interests – A firm must pay due regard to the interest of its customers and treat them fairly)* and act in Mr M's *best* interests under COBS 2.1.1R. Swan didn't ensure Mr M fell into one of the investor categories set out in COBS 4, nor was he treated as a professional client.

I think acting fairly and reasonably to meet its regulatory obligations, Swan should not have proceeded to make the promotion and arrange the investments in such circumstances. Were it not for the actions and misrepresentations of Swan, I think it's unlikely Mr M would have made the investment in Sooner Energy at all. So, I think it's fair to ask Kession to compensate Mr M for the loss he has suffered.

Putting things right

In assessing what would be fair compensation, I consider that my aim should be to put Mr M as close to the position he would probably now be in had he not been promoted the investment in Sooner Energy and had the arrangements not been made.

I think Mr M would have invested differently. It is not possible to say *precisely* what he would have done. But I am satisfied that what I've set out below is fair and reasonable given Mr M's circumstances and objectives when he invested.

What should Kession do?

To compensate Mr M fairly, Kession should:

- Compare the performance of Mr M's 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.

  Kession should also pay interest as set out below.

- Pay Mr M £100 for the trouble and upset caused by the loss of his savings and the uncertainty that has caused.

Income tax may be payable on any interest awarded.

Investment name	status	benchmark	from ("start date")	to ("end date")	additional interest
Sooner Energy	still exists (but illiquid)	FTSE UK Private Investors Income Total Return Index	date of investment	date of my decision	8% simple per year from date of decision to date of settlement (if compensation is not paid within 28 days of the business being notified of 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 (meaning it could not be readily sold on the open market), 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 M agrees to Kession taking ownership of the investment, if it wishes to. If it isn't possible for Kession to take ownership, then it may request an undertaking from Mr M that he repay to Kession any amount he may receive from the investment in future.

Fair value

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

Any withdrawal, income or other payment out of the investment 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 are a large number of regular payments, to keep calculations simpler, I will accept if Kession totals all those payments and deducts that figure at the end instead of deducting periodically.

Why is this remedy suitable?

I have chosen this method of compensation because:

- Mr M wanted capital growth on his savings and was willing to accept some investment risk.

- 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 better return.

- Although it's called an income index, the mix and diversification provided within the index is close enough to allow me to use it as a reasonable measure of comparison given Mr M's circumstances and risk attitude.

My final decision

My final decision is that I uphold Mr M's complaint against Kession Capital Limited.

To put things right, I direct it to pay to Mr M the fair compensation set out above. Kession should provide details of its calculation to Mr M in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 22 July 2022.

Ross Hammond
Ombudsman