

The complaint

Mr M complains, through his representative, about First Equity Limited. He's unhappy with the losses suffered on his portfolio and thinks that he's been given unsuitable advice and hasn't been treated fairly.

What happened

Mr M became an advisory client of First Equity in 2018. He'd followed his adviser there after he joined from another firm (Firm A). He complained to First Equity in 2020 and said, in summary, that the adviser hadn't correctly assessed his attitude to risk (ATR), hadn't kept him updated, had invested in unsuitable shares and traded excessively in order to earn higher commission. First Equity didn't uphold the complaint, so Mr M asked us to look into the matter.

The complaint was considered by one of our investigators who upheld it. He noted that Mr M had disputed most of the information the adviser had noted in the know your client (KYC) documents. He thought that Mr M wasn't in a position to take the level of risk that the adviser had recorded and pointed to a previous fact find stating he was a low-risk investor.

He didn't think Mr M's circumstances at the time - not many liquid assets outside of his portfolio and wanting to retire in a few years - left much time to recoup any major losses. He considered the calls Mr M had with the adviser about potential trades and didn't think he'd been given a chance to fully consider the risks associated with each trade.

First Equity didn't agree with his findings and said, in summary:

- If there had been a switch from lower risk investments to higher risk investments, then this happened before Mr M before their client and referred to the lack of information about what his ATR was in 2017 just before he became their client.
- Mr M had argued that the information in the KYCs was inaccurate. However, the risk profile had been completed in person and was signed by Mr M as being accurate. They'd had regular calls, meetings and emails with Mr M which would have given ample opportunity for him to consider his position and ask for the risk levels to be corrected. However, he did not raise any issues regarding his risk profile at any point.
- They didn't agree that the recommendations were unsuitable for Mr M. They highlighted that the section of the Fact Find where he answered 'no' when asked if he would face financial hardship if he lost the money he'd invested.
- They thought that Mr M understood what was being dealt with across his accounts. He'd dealt in the stock market for over 25 years and was a reasonably experienced investor. The KYC report he'd completed stated (regarding trades per month) that he had "dealt daily if appropriate", and therefore he would have known that the investments being proposed were not low risk investments.
- Mr M had access to an online system which would have confirmed the value of his

investments, in addition to receiving statements twice yearly.

- They had regular calls with Mr M, some of which were quite long in duration, where matters were discussed at length and showed that the adviser gave options when presenting trades.
- Mr M had brought a large portfolio when he became a client of First Equity which included a sizeable equity portfolio, not just investment/unit trusts and other lower risk investments. Mr M's portfolio continued to be dealt with in a consistent manner which did not indicate any change to his overall risk profile. If he was unhappy with the portfolio and the information provided in the KYCs, then any concerns or queries should have been raised at the time but they were not.
- KYCs were completed in 2018 and 2019 and Mr M signed to say that they were an accurate record of his financial situation, investment objectives and attitude to risk.
- They'd developed the KYC in accordance with COBS 9 – Suitability, and in doing so they'd paid due consideration to Mr M's knowledge and experience of the designated investments and/or services to be provided, his financial situation and investments objectives and attitude to risk. They were entitled to rely on the information and the KYCs stated that Mr M understood that the quality of their advice may be affected if he did not provide complete information. Therefore, it was reasonable for First Equity to rely on the KYC's contents.
- Their position was that Mr M's trading was suitable and in line with his risk profile. Any decision otherwise would not be fair or reasonable as all of the contemporaneous documentation indicated that Mr M classified himself as a high risk investor, or at the very least knew that he'd been so classified, and yet despite this (and despite being aware that the adviser was recommending higher risk investments) he didn't raise any concerns.
- If, despite their submissions, the complaint was still upheld, it would not be fair and reasonable for them to be held responsible for redress in respect of investments that were taken out on Firm A's advice. As such, they should only have to pay redress in respect of investments taken out by Mr M on their advice. Further, if Mr M really was a lower risk investor, at most redress should be based on a 50/50 split of the Income Total Return Index and the one-year fixed rate bond index.

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'd firstly think it may be helpful to point out that this decision doesn't address any of the concerns raised about the adviser's actions while he was employed by Firm A - it solely relates to his actions while at First Equity.

At the heart of this complaint is the issue of whether or not Mr M should have been advised to embark upon the adviser's chosen strategy. In order to determine this, I must consider his circumstances at the time. In addition to Mr M's testimony, I've also reviewed the documentation that was completed when he became a client of First Equity.

The KYC that Mr M completed said that he was aged 57, in full-time employment with a monthly disposable income of £6,150 and was looking to retire in seven years' time. He jointly owned properties valued at around £1,300,000 with an outstanding mortgage of

£151,000. He had 25 years investment experience and typically completed 20 trades per month with an average trade size of £20,000.

It noted that he had medium risk investments valued at £370,000, £330,000 with First Equity and the balance elsewhere. He had a medium risk portfolio with an asset allocation of 70% medium risk and 30% high risk. Regarding his attitude to risk and goals, it was noted that he:

- Wanted the best long-term returns he could get and expected periods where the value of the investments might suffer extended falls
- Wasn't concerned by falls in value and would expect to recover any falls by the time he sold his investments
- Wouldn't suffer severe financial hardship if he lost the money he'd invested

I note what Mr M has said regarding how the KYCs were completed. He's said, in summary, that the forms were completed by the adviser when he and his wife met him in a pub at short notice. The adviser filled in all the information whilst coaching the answers and had no interest in having an in-depth conversation about his financial plans or his true financial position.

I have no reason to doubt what he's said but I must also give weight to the written evidence. Mr M signed the KYC document to confirm, amongst other things, that the information was an accurate record of his circumstances and that the quality of the advice may be affected if he hadn't provided complete information.

That being said, I have taken into account the fact find he completed with Firm A in 2017 which recorded that his ATR was low. The 2018 KYC completed by First Equity said that his existing ATR was medium but didn't state which risk profile would be applied to his account. The 2019 KYC said his existing ATR was medium and his portfolio was made up of mostly FTSE Allshare stock with some Alternative Investment Market (AIM) stock, it also didn't state which risk profile would be applied to his account.

An adviser has certain obligations under the regulator's Conduct of Business Rules (COBS) rules and Principles for Businesses (PRIN). Some of the key rules I've considered in determining if the advice was suitable are:

COBS 9.2.1: which says, in summary, that a *firm must ensure that a recommendation, or a decision to trade, is suitable for its client. And when doing so, they must obtain sufficient information about the client's knowledge, experience, financial situation and objectives*

COBS 9.2.2: which broadly says, among other things, that a *firm needs to get enough information from the customer to be able to make sure the recommendation meets their objectives, they're able to bear any related investment risk and they understand the risks involved.*

COBS 9.3.1: 1) *A transaction may be unsuitable for a client because of the risks of the designated investments involved, the type of transaction, the characteristics of the order or the frequency of the trading.*

COBS 2.1.1R: *A firm must act honestly, fairly and professionally in accordance with the best interests of its client.*

PRIN 6: *A firm must pay due regard to the interests of its customers and treat them fairly.*

PRIN 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.

The strategy that the adviser recommended was to invest his entire portfolio with First Equity - nearly 90% of his available capital - in company shares, some of which were traded on the AIM. This had the impact of exposing Mr M's portfolio to a high level of volatility with the potential to make large losses very quickly. I don't think this was appropriate for his circumstances at the time, despite what was recorded in the KYCs completed by First Equity. He clearly had some investment experience and was recorded as a medium risk investor, but I think the strategy represented a significant increase in risk and I haven't seen where he was made aware of its potential impact.

I've also taken into consideration the impact of the charges generated by frequency of the adviser's trading activity - in 2019 alone there were around 426 trades resulting in charges of around £73,000 on a portfolio which was valued at £330,000 when it was transferred to First Equity. This was clearly significant and I haven't seen where the adviser made Mr M aware of the impact of his chosen strategy, which meant that there was potential for loss if the growth on the portfolio didn't exceed the cost of the charges.

Taking everything into account, I'm not persuaded that Mr M was in a fully informed position and I think the adviser's strategy exposed him to too much risk. I think he could have taken some risk but exposing his entire First Equity portfolio, which was the majority of his liquid assets to the risks created by direct equity trading - including AIM shares - wasn't suitable for his circumstances at the time, especially with the impact of the charges generated by the adviser's strategy and therefore First Equity must do something to put things right.

I note the points First Equity have made regarding any potential redress. But I don't see any reason to depart from the redress methodology the investigator proposed. I think it's fair to compare the return on Mr M's portfolio with a medium risk benchmark to try and fairly determine the return he would have received if he'd been suitably advised.

Putting things right

Fair compensation

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 if he had not been given unsuitable advice.

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

What must First Equity do?

To compensate Mr M fairly, First Equity must:

- 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 investments. If the *actual value* is greater than the *fair value*, no compensation is payable.
- First Equity should also add any interest set out below to the compensation payable.

Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Mr M First Equity Portfolio	No longer in force	FTSE UK Private Investors Income Total Return Index	Date transferred in	Date transferred out	8% simple per year on any loss from the end date to the date of settlement

Actual value

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

Fair value

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

Any additional sum paid into the investment should be added to the *fair value* calculation from the point in time when it was actually paid in.

Any withdrawal from the First Equity 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 First Equity totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically.

Why is this remedy suitable?

I have decided on this method of compensation because:

- Mr M wanted Capital growth 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 higher return.
- Although it is called 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

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £160,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £160,000, I may recommend the business to pay the balance.

First Equity Limited should provide details of its calculation to Mr M in a clear, simple format.

Recommendation: If the amount produced by the calculation of fair compensation exceeds £160,000, I recommend that First Equity Limited pays Mr M the balance plus any interest on that amount as set out above.

This recommendation is not part of my determination or award. It does not bind First Equity Limited. It is unlikely that Mr M can accept my decision and go to court to ask for the balance. Mr M may want to consider getting independent legal advice before deciding whether to accept this decision.

Determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My decision is that First Equity Limited should pay Mr M the amount produced by that calculation – up to a maximum of £160,000 plus any interest set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 23 March 2023.

Marc Purnell
Ombudsman