DRN-3996968

The complaint

Mr P complains that Crowdcube Capital Limited 'Crowdcube' gave him misleading information about a company ("A") he invested in through its platform. He wants Crowdcube to reimburse his losses.

What happened

Crowdcube operates an equity crowdfunding platform providing investing opportunities in small or start-up companies to investors in exchange for shares.

In March 2017, Mr P invested in A through Crowdcube's platform. As well as the funds raised through Crowdcube, A had a loan facility with a bank, B. The second tranche of this loan was due to be released a few months after the crowdfunding round. When the time came, B didn't release the additional funds because A hadn't met the revenue targets specified in the terms of the loan. Shortly afterwards, A was sold, resulting in Mr P making a substantial loss on his investment.

Mr P then discovered that, before the round of crowdfunding, A had breached another of the covenants of the loan. He complained to Crowdcube, saying it should have disclosed this breach in the pitch on its website, or the accompanying documents it sent him about A. He said it should reimburse his losses.

One of our investigators looked into things, and didn't think Crowdcube had done anything wrong. He said Crowdcube had warned Mr P the investment in A was high risk and that the company could fail. Also, on its website it also said investors should take care to carry out their own due diligence on prospective investments. As a result, he thought it had done enough to explain the risks of the investment and had presented information about A in a clear way. Mr P didn't agree and asked for an ombudsman to decide the matter, so the case was passed to me to decide.

My provisional decision

I issued a provisional decision on 3 February 2023 – I said I intended to uphold the complaint.

This is what I said:

The crux of this complaint is about the information Crowdcube provided Mr P about A. I've thought about Crowdcube's obligations under the Financial Conduct Authority's 'FCA's' rules. At the time of promoting A's investment opportunity, Crowdcube 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 principle here is:

- *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."*

Crowdcube 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 4.2.1R (1) "A firm must ensure that a communication or a financial promotion is fair, clear and not misleading."*

So before approving A's pitch, Crowdcube needed to satisfy itself that the information contained within it was fair, clear and not misleading. 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 so what these reasonable checks involve, or indeed what they might be in any given case, is something which is very much left to each platform to determine. In this circumstance, the level of due diligence Crowdcube carried out here isn't the issue. Instead, as the complaint centres on the fact that Crowdcube knew of the covenant breach, the question is whether Crowdcube ought to have included that information when it promoted the investment to Mr P and whether I am reasonably persuaded that had it done so, this would have made Mr P reconsider his investment in A.

I've borne in mind that the FCA said the following in 2015 when it issued a review of the regulatory regime for crowdfunding:

> *"Firms need to provide investors with appropriate information, in a comprehensive form, so that they are reasonably able to understand the nature and risks of the investment, and, consequently, to make investment decisions on an informed basis".*

One of the areas of concern the FCA identified was a situation where a platform provided:

> *"insufficient, omitted or the cherry-picking of information, leading to a potentiality misleading or unrealistically optimistic impression of the investment."*

I've also considered the FCA's guidance on approving financial promotions from November 2019 which explained that firms should:

> *"…analyse, and carry out due diligence regarding, the substance of a promotion before approving its content for communication by an unauthorised person. The extent and substance of the analysis and diligence needed to be able confirm that a promotion is fair, clear and not misleading will vary from case-to-case and will depend on the form and content of the promotion. When assessing whether a promotion is fair, clear and not misleading, a firm may need to consider (among other things):*
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> - *The authenticity of the proposition described in the relevant promotion."*

So Crowdcube needed to ensure any information it gave Mr P about A was fair, clear, and not misleading, and enabled him to make an informed decision whether to invest, armed with knowledge of the nature and risks of an investment into the company.

Whilst I appreciate Mr P had invested prior to the publication of the 2019 consultation paper and guidance, I still feel they are relevant as they provide clarity as to the interpretation and

application of the existing rules and guidance which were applicable to Crowdcube at the time.

Crowdcube provided Mr P with A's 'financial snapshot' as well as a 'legal explanatory note' with more information about the company. The explanatory note says A has an agreement to borrow a total of £3.5million from B. At the time of the crowdfunding raise, it had drawn down £2million of the facility, with the rest to be drawn down a few months later. The note proceeds to say the second tranche is dependent on A meeting revenue targets, that there are financial covenants in the loan agreement relating to A's cash and revenue, and that these covenants are in the process of being amended. The financial snapshot too, mentions the covenants and says A needs to hold specific levels of cash.

To my mind, making mention of the covenants and its renegotiation but failing to say why, or that they'd previously been breached, failed to give a full and clear picture of the loan arrangement. So, I don't think that it was sufficiently clear to allow Mr P to weigh up the risks and benefits of investing in A.

In addition, there is no indication from the information that was presented to Mr P that A held any concerns about achieving the loan covenants. Instead, it said it thought the money raised from the crowdfunding round should give it enough cash to meet its debt covenants for some time.

But in these particular circumstances I find that was misleading, because where the promotion details that A was reliant on a lending facility involving covenants relating to A's financial position, its ability to meet those covenants was a particular risk. So, I think knowledge of how A had performed against those covenants in the past would be a material factor in allowing investors like Mr P to make an informed choice about that risk, and whether it was one he was willing to accept.

In its response to this point, Crowdcube has said the first was a technical breach, and the latter was a different breach relating to the same covenant. So, two separate and unrelated breaches had occurred with the final resulting in the second tranche of borrowing being withheld. In addition, Crowdcube has maintained the explanatory note demonstrated the covenants were in the process of being amended, and investors like Mr P were encouraged to do their own due diligence.

I accept that the initial breach was unrelated, however I find that the promotion failed to give full context to the statements about the covenants. This was material information about A's viability and the risk that investing in the company presented. In my view, failing to mention this history meant Crowdcube failed to give Mr P the appropriate and necessary information to enable him to make an informed decision about whether to invest in A or not. So, I'm not persuaded Crowdcube communicated with Mr P in a fair, clear and not misleading way when it promoted A.

I'm satisfied Crowdcube didn't promote the investment in A to Mr P in a way that was clear fair and to misleading. So, the next question for me to consider is whether I think this omission would have affected Mr P's decision to invest. I've taken into account Mr P's submissions. He says he was swayed into investing based on the promotion. He understood that A was to receive the full loan arrangement from B and that A's ability to expand and grow was contingent on that arrangement, especially as the funds raised from the crowdfunding were to serve as a 'complement' to the debt finance. I'm therefore persuaded that any potential risks that this additional funding might not materialise, would've altered the prospect of A not succeeding as a company.

I find his testimony particularly convincing – Mr P was prepared to take the risk in A based on what the pitch was telling him. He hadn't been presented with any indication that A had failed to meet its loan covenants in the past, which otherwise would have led him to seriously consider the possibility that this might happen again in the future and therefore, the prospect of A's funding not materialising.

In light of this, I'm persuaded that had the promotion included detail of the breach, Mr P wouldn't have invested. So, I think Crowdcube should refund Mr P's investment into A, less anything he's received from the sale of the company.

Mr P responded to the provisional decision clarifying that he'd received a cheque for £159.30 on 14 June 2018 as payment for his shares after the sale of A. He confirmed the cheque hadn't been cashed.

Crowdcube didn't provide any new information or evidence for me to consider.

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.

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As Crowdcube has not made more comments or arguments for me to consider, I've got no reason to change the outcome I set out in my provisional decision.

I have noted Mr P's comments about the uncashed cheque from 2018. Crowdcube should note that if a cheque was previously issued to Mr P following the sale of A but remains uncashed, the cheque is unlikely to remain valid. It should however be cancelled, and so this amount shouldn't be deducted from the overall redress.

To confirm, for the reasons described in my provisional decision, I find that Crowdcube failed to provide Mr P with clear, fair and misleading information when promoting A. But for these failings, I don't think Mr P would have invested. I uphold this complaint.

Putting things right

To put things right, Crowdcube should put Mr P in the position he'd have been in had he not invested. It should therefore refund to Mr P the amount he invested in A, less anything he's received from the sale of the company.

My final decision

For the reasons set out above, I uphold this complaint. My decision is that Crowdcube Capital Limited should pay the amount calculated as set out above.
Under the rules of the Financial Ombudsman Service, I'm required to ask Mr P to accept or reject my decision before 31 March 2023.

Farzana Miah
Ombudsman