

The complaint

Mr and Mrs Y have complained that Amersham Investment Management Ltd ('AMIM') didn't comply with its own investment criteria or carry out the proper due diligence before it invested their funds into enterprise investment schemes ('EIS'). Mr and Mrs Y have lost their total investment of £133,505 and would like this returned to them with interest.

What happened

Mr and Mrs Y wanted to reduce a capital gains tax bill by investing into EIS funds. Their independent financial adviser ('IFA') didn't have the necessary expertise to advise Mr and Mrs Y about this. To facilitate Mr and Mrs Y's requirements their IFA met with a third party – who I shall refer to as 'K' in the decision – which was a platform offering funds that invested into EIS and similar. After reviewing what was being offered, Mr and Mrs Y and their IFA chose a variety of funds for investment.

AMIM acted as fund manager for two of the funds chosen;

- Odexia Consumer Brand EIS Fund ('Odexia')
- Amersham Corporate Development Capital EIS Fund ('ACDC')

Mr and Mrs Y became dissatisfied with how the above two funds were managed, and they didn't think that AMIM had invested into the underlying EIS as it said it would.

For the Odexia Fund they were unhappy with two investee EIS invested into, who I shall refer to as 'CN' and 'CP' in my decision, and for the ACDC Fund they were unhappy with an investment into an EIS I shall refer to as 'BI' in my decision. They complained to AMIM in February 2023.

AMIM responded to Mr and Mrs Y's complaint. It said;

- Mr and Mrs Y's investment adviser assessed that their investment – into higher risk EIS funds – was appropriate for them bearing in mind their financial circumstances and risk profile etc.
- AMIM explained that the nine-point investment criteria Mr and Mrs Y had referred to didn't apply to the dates their investments were made. It detailed the aims and investment requirements in the relevant Information Memorandums that did apply.
- It addressed the complaint points made about the three EIS referred to, as much as they were relevant to the updated Information Memorandums.
- It also explained its relationships with third parties – its investment advisers – who it said had the experience and expertise in the relevant sector. It was the investment advisers who had carried out the due diligence and who could add value to the businesses invested into. It said it was entitled to rely on third party due diligence.
- In conclusion, AMIM didn't uphold Mr and Mrs Y's complaint.

Unhappy with the outcome to their complaint Mr and Mrs Y brought it to this service. They said;

- They had relied upon the Investment Summary document provided to them by AMIM which included the Investment Strategy and nine-point investment criteria that their investments were being managed in their best interests. But they say the Investment Strategy wasn't complied with when investing in CP and CN and AMIM were negligent in its due diligence.
- Mr and Mrs Y outlined where the Investment Summary criteria hadn't been met for both the investments.
- Mr and Mrs Y also weren't happy with the BI investment within the ACDC Fund. They say there wasn't any significant sales activity and so BI didn't meet the necessary Investment Summary criteria.

Our investigator who considered the complaint didn't think it should be upheld. He said;

- He didn't investigate the advice or the suitability to invest as that was provided by Mr and Mrs Y's IFA.
- He did consider whether AMIM carried out sufficient due diligence and whether it managed Mr and Mrs Y's investment in line with its terms and conditions and the Information Memorandum.
- AMIM used third parties to carry out the due diligence prior to the investments. It followed a process to satisfy its internal commercial decision to invest and the investigator thought it wasn't unreasonable for it to rely upon the third parties' expertise and findings.
- Regarding Mr and Mrs Y's concerns about the three holdings – CP, CN and BI – he would have expected for Mr and Mrs Y's IFA to have researched both ACDC and Odexia before investing in them. Information about both funds was available to Mr and Mrs Y prior to investment and he was satisfied Mr and Mrs Y, through their IFA made an informed decision.
- AMIM weren't responsible for the advice, risk assessment or research – that would have been for Mr and Mrs Y's IFA and K.
- Mr and Mrs Y had lost money due to the performance of the investments, however that wasn't due to AMIM's management of the two Funds but to do with the performance of the underlying investee EIS. The investments were high risk.

Mr and Mrs Y didn't agree with the investigator. In their response they said;

- The Investment Summary constituted a contract between the manager and the investor. And that was breached.
- Mr and Mrs Y had chosen AMIM to invest with because of its nine-point criteria before investing in an underlying EIS qualifying business within the Funds. AMIM hadn't invested within those criteria, so the contract was breached.
- AMIM had a duty of care to check the due diligence carried out on its behalf by third parties.
- The investigator hadn't provided any evidence that AMIM and associated parties had carried out any specific due diligence to ensure those investments complied with its own criteria.

The investigator confirmed that he was satisfied with the due diligence that had been carried out and it was reasonable for AMIM to follow the third parties' guidance. It wasn't the role of this service to question AMIM's commercial decision.

Mr and Mrs Y disagreed. AMIM had a duty of care to ensure the investee EIS complied with its investment criteria. It wasn't reasonable for it to rely on due diligence carried out by third parties. AMIM were either negligent in its due diligence or provided misleading promotional information to investors. Mr and Mrs Y had suffered financial harm because the financial promotion material was unclear and/or misleading.

As the complaint remains unresolved, it has been passed to me for a 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 should first explain that this service is an informal dispute resolution service set up as a free – to consumers – alternative to the courts. In deciding this complaint, I have focused on what I consider to be the central issues that are relevant to the outcome of the complaint, rather than commenting on every issue in turn. This isn't intended as a discourtesy, rather it reflects the informal nature of our service and my remit.

And I'm aware I've set out the background to this complaint in far less detail than the parties and I've done so using my own words. I've focused on what I find are the key issues here. Our rules allow me to take this approach. It simply reflects the informal nature of our service. I'm satisfied I don't need to comment on every individual argument to be able to reach what I think is the right outcome.

The due diligence carried out by the third parties

AMIM appointed third parties – investment advisers – to carry out the due diligence and in my view, it wasn't unreasonable for AMIM to place reliance on a third-party adviser's selection of suggested investments who had experience and expertise in the particular sectors and who in its opinion had the relevant experience to do so and could add value to the investee businesses. But and I agree with Mr and Mrs Y on this point, the final assessment and decision whether to invest was for AMIM.

So, while AMIM used the services of its investment advisers to introduce potential investee businesses and carry out the due diligence as to whether they were a good investment prospect, it was AMIM who was ultimately responsible for that decision to invest. AMIM is entitled to ask for third parties to carry out that due diligence as part of its process but in its role as the fund manager, the decision to invest in the underlying business, was AMIM's alone.

And Mr and Mrs Y didn't have any relationship with the investment advisers carrying out the due diligence. It was AMIM who had the relationship with Mr and Mrs Y – and the responsibilities implicit in that relationship – and not the investment adviser.

However, I would also say, from the evidence available to me, including the due diligence documents AMIM has provided, there is nothing to indicate that it wasn't carried out appropriately or without care.

That being said, EIS are high risk investments and any decision to invest made by the fund manager based on information received, and in good opinion, can sometimes go wrong.

That is just the fund manager's legitimate use of judgment. As AMIM was the discretionary manager of the Funds being complained about it was for AMIM to make legitimate commercial decisions on behalf of investors based on the information available at the time.

And based on the evidence I've seen I'm not persuaded that AMIM failed to make decisions in line with the investment objectives of the respective funds.

In making their complaint Mr and Mrs Y have referred to the Investment Summary and the nine-point criteria that the fund manager was to use to be satisfied the investee business met before it decided to invest. Mr and Mrs Y said that these criteria gave them confidence that the Funds were being managed in their best interests.

Mr and Mrs Y say that AMIM's failure to meet each of its own criteria should have stopped the investments going ahead or investors should have been made aware and given the option whether to invest. But not all of the points Mr and Mrs Y complained about applied to the new updated Information Memorandum. Mr and Mrs Y were referring to an outdated Investment Summary that didn't apply at the point of investment.

Complaint about Odexia

In response to Mr and Mrs Y's complaint AMIM confirmed the Information Memorandum for the Odexia Fund that applied to Mr and Mrs Y's complaint was dated 15 March 2016. That document confirmed;

'The aim of the Fund is to focus investment on businesses which have established revenues, are growing strongly, have high growth potential and are planning to exit within five years.'

The Information Memorandum referred to other points of consideration for prospective opportunities – the objectives of the Funds;

- Investing into emerging consumer and leisure brands where its investment advisers could add value to improve growth, build the brand and add value.
- To invest into businesses that had been trading for 12 months with a monthly revenue of up to £500,000.
- Growth, or the potential for growth, of around 25% per annum, along with
- good management teams.

There were three 'investment restrictions' but these related to the investee company;

- Assurance that HMRC was satisfied the shares of the investee company would meet EIS scheme requirements.
- Approval from the manager.
- Appoint a non-executive director if required by the manager.

In its response to the complaint points made about CP, AMIM said that during the due diligence process the assumed growth rate for CP had been 25% per annum but those were just forecasts, even if they were backed up by reasonable assumptions during the due diligence process.

For the investment into CN, Mr and Mrs Y said that the business was not achieving breakeven as quoted in the Investment Strategy as being a requirement and were also concerned about the valuation of the company taking account of its capital and reserves.

From the information I have seen, it wasn't a requirement that a business needed to be breaking even prior to investment. And regarding the valuation, AMIM explained this had been established by the due diligence investment advisers, but for earlier stage businesses it wasn't unusual to use sales multiples for valuations and it provided further financial details.

Complaint about ACDC Fund

Mr and Mrs Y complained that at the time of investing, BI wasn't breaking even, and it was a research and development business at the time.

The relevant Information Memorandum for the ACDC Fund was dated 25 January 2016. The 'Investment Objective' overview for the Fund states;

'ACDC seeks to mitigate risk and maximise profits by combining a deep review and understanding of the inherent technology and IP [intellectual property] of the target companies which have been developed into businesses generating revenues...The Manager's objective is to maximise returns for investors by investing into target companies of diverse characteristics while a focused view can be maintained on the investments...'

The same 'investment restrictions' were to be applied to the investee business as referred to above.

In its response to the complaint AMIM said that BI was generating small scale revenues but had intellectual property and other intangible assets which made it a business that could be benefit from ACDC's involvement.

In reviewing the above, I haven't commented in any great detail about either Mr and Mrs Y's complaint to AMIM or its response – both of which dealt with individual and particular points about Mr and Mrs Y's rejection of the reasons for investment and AMIM's subsequent explanation as to why the investment had gone ahead. But the responses seem to reasonably address the complaint points made and the purpose of this decision is to set out my view on what I think is fair and reasonable in the individual circumstances of the complaint, and not to offer a point-by-point response to everything the parties have said.

In respect of each underlying investee EIS, with reference to the due diligence, I've seen that an assessment was made of the core information surrounding the underlying companies' financial affairs and forecasts, discussions with the directors and the eligibility for EIS qualifying status, etc. And copies of those documents were provided to AMIM.

While it's not my role to be prescriptive about the level of due diligence that should be carried out, I haven't seen anything to suggest that it wasn't carried out to a reasonable standard. I appreciate Mr and Mrs Y haven't seen these commercially sensitive documents but there's no regulatory requirement for a fund of this type to disclose reports to them.

I haven't been given anything to suggest that the investments themselves were so far outside of the investment remit or objectives as confirmed in the Information Memorandums of the relevant funds for me to reach a conclusion that it was unreasonable for the fund manager to have invested. I say this because fund managers have a wide discretion to invest as they see fit. So even though an investor may not have agreed with those investments, it was a decision for the fund manager to make whether investment should be made provided the fund manager considered they were suitable for the objectives of the funds.

Given that there had been an assessment as to viability of the companies by a third-party investment adviser with industry knowledge, that the companies were operating as set out in the Information Memorandums and within the industry sector, as well as having EIS qualifying status, there's nothing to show that it was unreasonable for AMIM to have approved these companies for investment at the time.

However, even if the conclusions reached in the due diligence operations – that the respective businesses were suitable for the AMIM Funds and AMIM agreed – subsequently led to an investment decision which turned out to be wrong – in that it didn't prove to be successful – that wouldn't necessarily cause me to uphold the complaint.

I say this because of the high-risk nature of the EIS investments. And by investing into those – even by reducing the risk by investing via a fund rather than direct investment – will inevitably expose the investor to the unpredictability's of high-risk investment and the potential pitfalls that can result in.

And provided a fund is invested in line with its overall objectives then it wouldn't be fair or reasonable for me to uphold the complaint on this point. I haven't seen anything to suggest that the funds were invested outside of their stated investment objectives or risk profile.

While I can understand why Mr and Mrs Y aren't happy with the performance of the two funds, but the issue of fund performance in itself is not something I can consider and is not straightforward. The funds that Mr and Mrs Y invested in were actively managed – the money was invested in investee businesses chosen by fund manager, AMIM. If the fund performed poorly that's because the fund manager had taken certain decisions that hadn't paid off. That's disappointing, of course, but reflects the fund manager exercising their judgement – which they're supposed to do.

In conclusion, the fact that the investee businesses invested into by AMIM within the two funds went on to fail is not indicative itself of a failing in the due diligence process or non-compliance with the objectives of the funds. It's important to put into context that EIS are non-mainstream, complex, illiquid, specialised and speculative investments, where there is always a real risk of losing the original, capital investment. These were new businesses where the risk of failure was higher; it was this higher level of risk which justified the availability of generous tax reliefs. And from what I have seen, I'm satisfied that the due diligence carried out, and which AMIM is ultimately responsible for, wasn't of an unreasonably standard.

So, taking all of the above into account, I don't uphold Mr and Mrs Y's complaint. No doubt they will be disappointed with my conclusion – it's clear they feel strongly about their complaint. But I hope I have been able to explain how and why I've reached the decision that I have.

My final decision

For the reasons given, I don't uphold Mr and Mrs Y's complaint about Amersham Investment Management Ltd.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs Y and Mr Y to accept or reject my decision before 25 April 2024.

Catherine Langley
Ombudsman