DRN-4595870

The complaint

Mr C complains about the price he was given on certain Contract for Differences (CFD) trades which Spread Co Limited closed. He believes he wasn't given the right price and this caused him a financial loss.

What happened

On 26 January 2022 Mr C had some open CFDs on the share price of a company I'll call 'F' – this position amounted to around 28,000 shares in F.

At market open on 26 January 2022, the share price of F fell significantly on the back of some newly released financial data, and this caused Mr C's account to have less than the 50% margin required to keep his position open. As a result, under the terms of his account his entire position of 28,000 shares was now at risk of being liquidated by Spreadco.

Spreadco has explained that at the time, Mr C's position was 14 times the Exchange Market Size (EMS – what Spreadco says is the 'normal trading size of the [underlying] stock'). At market open, trading in F's shares was temporarily suspended for 5 minutes. Trading resumed between 8:05 and 8:10, during which the time the average trade size was 400 shares, but over 282,000 shares in F were traded. F's shares then went into auction just before 8.11 and were then reopened for trading at just before 8.16. Mr C's position was closed at 8:10, a few seconds before the auction. His trade was initially booked on his account at a price of 754.48p, but was then amended post-execution to 693.6882. Spreadco says the original price was a mistake and said Mr C's position was filled at the second price. Mr C complained.

One of our investigators looked into Mr C's complaint but didn't think Spreadco had done anything wrong. It said Spreadco's actions were consistent with the terms of the account, and it had given him the price it had achieved in the underlying market.

Mr C didn't agree and provided a detailed response that was produced by another broker.

In short, this said:

- Mr C had a similarly sized position of around 22,000 shares with this other broker, and it had managed to close his position at 8:06 at a price of 752.4.

- Mr C's account with Spreadco went into liquidation at around the same time, at 8:06, and there was almost 5 minutes of trading during this time. It said that there was sufficient liquidity in the market between 8:05 and 8:10, because over 282,000 shares were traded.

- It said that Spreadco hadn't explained why it took so long to fill Mr C's order, and it said if it had acted sooner, it's likely Mr C would've received a better price.

I asked Spreadco for its comments on Mr C's submissions. In summary it said:

- There was insufficient liquidity in the market between 8:05 and 8:20, and this was demonstrated by the average trade size being 400 shares.

- It didn't consider the fact that another broker had been able to execute similarly sized trade relevant because 'his equity liquidity level for the positions he held would vary between brokers' and other 'brokers may have the option to work multiple exchanges for liquidity for which we cannot comment and varying execution policies'.

- It provided an email exchange, post execution, with its counterparty in which it asked for guidance on how to dispose of such a large quantity of shares in these sorts of market conditions. It said that Spreadco would usually place an order at market 'to exit a hedged position upon liquidation of a client's position' but due to the circumstances, Spreadco 'did not attempt to place a market order, with the foresight that it would be irresponsible given the market conditions and that it would most likely be rejected'. It said that the counterparty confirmed this when it said that this is what would've happened – the order would've been rejected.

- It said it wasn't practical to place limit orders given the high volatility and illiquid market conditions. It therefore asked the counterparty if the 'responsible approach to disposing of the shares would be to allow the order book to populate further and the volatility to subside' and the counterparty confirmed that it would be.

- It therefore concluded that its actions were consistent with the above and aligned with the guidance from its counterparty. It said that the order was subsequently placed, and the fill it was given by its counterparty broker was 693.6882 which is what it passed on to Mr C.

- It said that the price of 754.48 which Mr C was initially given was an error, and the reversal of the trade was consistent with the terms.

- It concluded by reiterating that that it was Mr C's responsibility to monitor his account and ensure it was adequately funded in order to prevent the liquidation of his instruments.

I issued a provisional decision in January 2024. In it I said:

When I asked the investigator to write to Spreadco and give it an opportunity to consider Mr C's additional submissions, I also gave it an indication that I thought Mr C's complaint should be upheld. I'd like to thank Spreadco for considering what Mr C has had to say, but I don't find its response persuasive and, for the reasons below, I remain of the view that Mr C's complaint should be upheld.

However, I have explained in detail my reasons. I should make clear that this is a provisional decision, and I will take into account any comments I receive by the deadline before issuing my final decision.

I've firstly set out the applicable standards, and any relevant terms from Mr C's agreement with Spreadco. I've then gone on to explain why I consider his complaint should be upheld, and how I think Spreadco needs to put matters right.

The applicable standards

In addition to the Financial Conduct Authority's (FCA) High Level Principles, which apply to this case, I consider the following standards are also relevant.

The FCA's Conduct of Business Rules (COBS) set out the rules which Spreadco was required to follow.

COBS 11.2A.2 sets out Spreadco's obligations to take 'sufficient steps to obtain, when executing orders, the best possible results for its clients taking into account the execution factors'. These factors include 'price, costs, speed, likelihood of section and settlement, size, nature or any other consideration relevant to the execution of an order'.

COBS 11.2A.29 says:

'An investment firm executing orders should be able to include a single execution venue in their policy only where they are able to show that this allows them to obtain best execution for their clients on a consistent basis. Investment firms should select a single execution venue only where they can reasonably expect that the selected execution venue will enable them to obtain results for clients that are at least as good as the results that they could reasonably expect from using alternative execution venues. This reasonable expectation must be supported by relevant data or by other internal analyses conducted by investment firms.'

COBS 22.5.13 explains the requirement for Margin close out for retail clients:

(1) A firm must ensure a retail client's net equity in an account used to trade restricted speculative investments does not fall below 50% of the margin requirement (as outlined in COBS 22.5.11R) required to maintain the retail client's open positions.

(2) Where a retail client's net equity falls below 50% of the margin requirement, the firm must close the retail client's open position(s) on restricted speculative investments as soon as market conditions allow.

And COBS 22.5.16 specifies that firms 'are reminded that they must comply with COBS 2.1.1R (the client's best interests rule) and COBS 11.2A.2R (obligation to execute orders on terms most favourable to the client) when:

(1) Making a margin call to a retail client; or

(2) Exercising a discretionary right to close a retail client's position; or

(3) Closing a retail client's position(s).

Spreadco has a 'Best Execution Policy'. In it, it says that it is a 'market maker for Contracts for Difference and Spread Betting products' and 'acts as principal in all orders placed with all its clients'. It says that this means 'client orders are not passed on to or executed on a third party venue'. It says that it 'creates its market prices by sourcing them from multiple venues and adding a spread to them, ensuring that the prices are fair and current'. The policy also says that orders submitted to Spreadco will be 'checked to ensure liquidity of the underlying market (e.g. for orders outside the normal trading size)'. It says that 'if the liquidity is not available in the underlying market the order may not be executed at the requested price or may be subject to a requote'.

Mr C and Spreadco also had an agreement in place for the services Spreadco was providing. Of relevance to this complaint I've noted the following terms:

3. Trading with Spread Co

3.1. When executing Trades, or carrying out other actions pursuant hereto, Spread Co will *act as principal and not as agent on your behalf.*

8. Maring requirements

8.11 Where you fail to meet a Margin Call, you acknowledge and agree that Spread Co has authority to take such action as it considers in its absolute discretion to be necessary or desirable in order to reduce or limit your exposure and Spread Co's exposure, as more particularly described in clause 9.4 below.

9. Closing positions

9.4. Spread Co has discretion to close all or part of your position represented by your Open Trades immediately, without giving you any notice, where at least one of the following applies:

- *b) you fail to meet the Margin requirements for all your Open Trades from time to time.*

20. Conflicts of interest

20.3 We have also detailed the following conflicts that may exist due to the nature of the services provided:

- *a) we may (but are not obliged to) effect hedging strategies or transactions in order to manage risk inr elation to trades you make, or may make. This may impact the price at which you enter into Trades and any profits generated by such strategies may be retained by us;*

- *d) we fully deal in underling markets for which your Trades relate as principal (for your own account).*

My provisional findings

In looking at the evidence available, I'm not persuaded that Spreadco has acted consistently with its obligations under COBS or its own agreement with Mr C.

At the point that Mr C's account had less than 50% of the required margin to keep his positions open, COBS required Spreadco to take action, as long as market conditions allowed. Whilst I note its submissions about the volatility and relative illiquidity of F's shares, it's clear that there was trading in the market. I say this for the following reasons:

- *Mr C has supplied evidence from another broker who closed a similarly large position at 8:06 without this materially affecting the market, the price or the liquidity available.*

- *Mr C has also supplied evidence demonstrating the overall trade volume during that same time period as being far in excess than the position he had open with Spreadco.*

- *Spreadco itself has not denied that trading was taking place between 8:05 and 8:10, nor that its first attempt at closing Mr C's position happened at 8:10.*

Waiting for 5 minutes before taking any action on Mr C's account, when shares were being traded and the market was open, was not in my view consistent with Spreadco's obligations to take action. Furthermore, it was also not consistent with its obligations to provide Mr C with best execution.

Spreadco has confirmed that usually, in the event of a margin close out, it would place a market order with its counterparty to exit a hedged position. It says that it chose not to do this in Mr C's case because it would've been 'irresponsible'. But it's clear to me that the fill it eventually gave Mr C was not the best available price at the time when Mr C's account had insufficient margin. He obtained a much better price 5 minutes earlier than Spreadco's execution of his order, for a similarly sized trade, and the evidence from the pricing data I've seen shows that the prices were consistently better in the intervening 5 minutes before 8:10, than the fill he received.

Spreadco has provided evidence from its counterparty that says it would've rejected an order of this size given the market conditions – but I'm not persuaded by this evidence. First of all, this email exchange occurred in response to me making further enquiries – it was not something that happened at the time. Secondly, the evidence I've seen and referred to above shows that trades, of a very significant size, were clearly able to be filled at the time – and I'm not persuaded that waiting whilst a client's losses increased, and they fell further below the required 50% margin, was the fair and reasonable thing to do. I'm equally not persuaded it was in Mr C's best interests. I say this because Spreadco had to weigh up the risk of reducing Mr C's exposure to the market as soon as market conditions allowed, under COBS, and the desire to see the market stabilise. It's clear to me that at that moment in time, given the size of Mr C's position, it wasn't fair and reasonable to prioritise better market conditions over the possibility of Mr C's losses increasing even further, as they in fact did. Spreadco has dismissed Mr C's evidence from another broker on the basis, in summary, that all brokers are different and do things differently. But whilst that might be true to a certain extent, I'm not persuaded that's material here. Mr C wasn't trading forex, he was trading a CFD on a listed share. It seems to me that the only material difference between Spreadco and the other broker is that Spreadco was not, in fact, dealing in the underlying market – it was placing an order with a counterparty, who would then deal in the underlying.

It isn't my role to question how Spreadco decides to deliver its service, but from the terms of its Best Execution Policy, and the Terms and Conditions of the account, I'm not persuaded this is what it had agreed with Mr C it would do.

The agreement with Mr C, which includes its commitment to provide to him best execution, clearly says that Spreadco will act as Principal. It also says that Spreadco will deal in the underlying but at least in relation to Mr C's CFDs in F, that's not what it did – it had a counterparty through which a trade would be placed, and it was the extent to which this counterparty was happy to trade with Spreadco which dictated whether not Mr C's trades would be closed.

Furthermore, Spreadco also gave itself discretion to close all or part of a position in the event of margin default – but it did neither of these things for a full 5 minutes in Mr C's case. The only reason it has given for not exercising its discretion was that it would've been irresponsible on the basis that the trade would've been rejected – I'm not persuaded by this. Having a trade rejected would've simply confirmed that it had tried to execute Mr C's trade as soon as it could – or it may have encouraged it to attempt to part fill Mr C's order. Both of these scenarios in my view would've demonstrated greater adherence to COBS and the terms of the account than not doing anything until 8:10.

Ultimately, the crux of the complaint here is that Spreadco was considering its ability to hedge Mr C's position in the market – and not whether or not it could in fact close Mr C's trade, given that he was trading (as the terms are explicit about) with Spreadco as principal. The issue is really only about the price Spreadco was quoting or giving to Mr C, and its own trade via its counterparty would've given evidence of that – as it did for its trade at 8:10. But the dispute isn't around the price it gave Mr C at 8:10. The dispute is around whether it could've closed Mr C's position earlier, and if it had, whether he would've received a better *price than he did at 8:10.*

As I've said above, as Spreadco did not attempt to carry out any trades in the underlying market between 8:05 and 8:10, I can only rely on Mr C's evidence – which I've referred to above. And on balance, I'm satisfied the evidence shows that it's more likely than not that Spreadco could've closed Mr C's trades earlier than it did – and he would likely have received a better price than what it eventually gave him.

Taking everything into account, I'm not persuaded Mr C was given the best available price for his position. I'm not convinced there was anything 'irresponsible' in Spreadco attempting to reduce Mr C's exposure as soon as he had insufficient margin and consider that this is exactly what COBS required Spreadco to do. Whilst I accept market conditions were challenging, I'm not persuaded it's fair and reasonable that Mr C bear the financial consequences of Spreadco deciding not to take any action on his account for 5 minutes whilst F's share price continued to fall.

Putting things right

In order to put things right, I've considered the evidence available. In my view, given Mr C received a fill of around 752.4 at 8:06 that is the most likely price he would've received had Spreadco carried out the same trade, as soon as Mr C's account went into margin deficit. I say this because its quote of 754 occurred at about the same time – but without Mr C's trade having been placed. Given the situation, I consider that placing two very large orders (the one with Spreadco and the one with Mr C's other broker) in a short period of time would most likely not have improved the price Mr C received on his Spreadco position – so I don't think 754 would've been achievable.

I can't say with any likelihood whether it would've meant a worse fill than what he received with the other broker – so I'm satisfied that asking Spreadco to give him the same price is fair and reasonable given the similarities in volume and timing.

This means that Spreadco needs to refund the difference between the fill it gave Mr C on his 28,000 shares in F, and the price of 752.4 which is the price he could've received had Spreadco given him the best available price at market open.

Responses to my provisional decision

Mr C agreed with my provisional conclusions. Spreadco provided some more information. In short, it said that it wouldn't have been able to close Mr C's trade all in one go at the price I specified in my provisional decision. It provided evidence of the prices available and said that it would've taken around 3 minutes to close his position in its entirety. It therefore said that a fair and reasonable way of calculating the price he would've received was to base it on the average of the available prices at the time. This was 736.91.

I considered Spreadco's new submissions and amended my proposal for putting things right. I wrote to both parties and said the following:

'*I've taken on-board the business's comments and have decided that the following method is fair and reasonable, and more reflective of what would've happened at the time had Spreadco acted as it should have done.*

As I said in my provisional decision, I accept that at the time there was low liquidity and it's unlikely that Mr C would've received a better fill from Spreadco had it acted as it should've done. I provisionally concluded that, in the absence of any other evidence, I couldn't say whether Mr C would've received a worse fill had Spreadco executed his trade at 8:06.

However, on reviewing the circumstances and Spreadco's comments, I've accepted that it would've taken Spreadco a few minutes to carry out Mr C's trade – this was a larger trade than the one he had with IG, and I accept the circumstances weren't straightforward. It's important that I emphasise to Mr C that the fact a different broker did things quicker or differently is not determinative of his case, and there will be a range of factors that each broker faces when executing trades of this size, and in such challenging circumstances.

Having considered Spreadco's comments, I agree that on balance, it's more likely than not that Spreadco would've needed to close Mr C's position in tranches. To that end, I agree that a fair and reasonable way of quantifying Mr C's losses it to use an average price, but I disagree with Spreadco's method and instead I intend to recommend the following:

Mr C has provided evidence that a trade in the underlying market achieved a price of 752.4 at 8:06, around the same time as Spreadco says the process for his stop-out was initiated. I think this price ought to form part of the average, as that was clearly an achievable price for at least some of Mr C's order.

I've then used the next four available prices, which Spreadco has provided, over the course of three minutes, as I agree it's likely this is a reasonable timeframe for when Spreadco would've carried out the relevant trades and eventually closed Mr C's position.

This means that I intend to direct Spreadco to:

- *Pay Mr C the average price between 8:06 and 8:09:*
  - *752.4*
  - *748.6*
  - *741.6*
  - *741.5*
  - *721*
- *The average price would've therefore been 741.02 – so in my final decision, I intend to direct Spreadco to compensate Mr C for the difference between the fill it gave Mr C on his 28,000 shares in F, and the price of 741.02, which is the average price he most likely would've received had Spreadco acted as it should have.*

The remainder of my provisional findings remain unchanged.'

Mr C accepted my provisional decision and my revised method for putting things right. Spreadco didn't agree.

It said that it still maintained, given the circumstances of low liquidity and other brokers selling the same shares due to their clients liquidtions, the best it could have achieved would have been an average execution price of 736.91. It said that this was its conclusion and it had provided all the evidence it had to justify it.

It said that Mr C was aware of the risks of investing in illiquid markets, and the matter could've been avoided had Mr C had added additional margin to his account at the time.

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.

As Spreadco didn't provide any comments in response to the substance of my provisional findings, I confirm them here as final. Therefore the final matter to decide is how to put things right for Mr C.

Putting things right

I acknowledge Spreadco's position about the best price it would've reasonably been able to achieve for Mr C. But the evidence it has provided isn't inconsistent with what I suggested would be a fair and reasonable price – and Mr C has also provided evidence which I've taken into account.

Having reconsidered all the evidence, and each party's relevant submissions, I'm satisfied that my revised proposal for putting things right is fair and reasonable and ensures Mr C is put in the same position he likely would've been in had Spreadco provided best execution to him.

So I've accepted that, on balance, it likely would've taken Spreadco a few minutes to carry out Mr C's trade – this was a larger trade than the one he had with IG, and I accept the circumstances weren't straightforward. And I'm persuaded that on balance, it's more likely than not that Spreadco would've needed to close Mr C's position in tranches. So I consider that a fair and reasonable way to quantify Mr C's losses is to use an average price.

Mr C has provided evidence that a trade in the underlying market achieved a price of 752.4 at 8:06, around the same time as Spreadco says the process for his stop-out was initiated. I think this price was clearly an achievable price for at least some of Mr C's order. Spreadco has then provided evidence of the next four available prices over the course of three minutes – I'm satisfied this is a reasonable timeframe to use given the circumstances. This means that broadly speaking, Mr C's overall financial loss is the difference between the average price he most like would've received between 8:06 and 8:09 and the price Spreadco eventually gave him.

- The relevant prices between 8:06 and 8:09 for the purposes of this calculation are:
    - 752.4
    - 748.6
    - 741.6
    - 741.5
    - 721
- So the average price would've been 741.02. Spreadco therefore needs to compensate Mr C for the difference between the fill it gave Mr C on his 28,000 shares in F, and the price of 741.02, which is the average price he most likely would've received had Spreadco acted as it should have.

My final decision

My final decision is that I uphold this complaint. Spread Co Limited must pay the compensation I've outlined above to Mr C within 28 days of when we tell it he has accepted this final decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr C to accept or reject my decision before 6 March 2024.

Alessandro Pulzone
Ombudsman