DRN-4878172

The complaint

Mr S complains he was mis-sold a minibond investment by EGR WEALTH LIMITED (formerly EGR Broking). He says he was recommended an investment that was high-risk and not suitable for his circumstances and has suffered losses as a result.

What happened

Between May and June 2020, Mr S invested around £17,000 over three transactions in a minibond product to be held in a general investment account. He was due to receive interest at a rate of 8.1% per annum, with payments due to be paid twice a year in June and December. The investment was due to mature in December 2022.

Mr S was introduced to the opportunity by EGR. He completed the required application paperwork it provided – this included a suitability and appropriateness test. As part of the application he signed a declaration to indicate he was a high net worth (HNW) investor.

In 2022, problems emerged with the investment as there were delays in payment of interest. In May 2022, EGR sent investors an update from the bond issuer, which apologised for the lack of communication regarding interest payments and explaining further issues with the performance of the investment. Then in September 2022, EGR sent Mr S notification that the bond issuer had been placed into administration as of 1 August 2022.

In December 2022, Mr S raised a complaint with EGR about the mis-selling of his investment. EGR responded but didn't uphold the complaint. In summary it said:

- EGR did not advise Mr S, it only provided an "Execution Only" service and the documentation is clear that was the basis of the transaction. So there was no requirement upon EGR to assess Mr S for his suitability for the product.

- Based on the information that EGR received at the time about his circumstances, Mr S appeared appropriate for the product. EGR carried out the necessary due diligence by providing Mr S with the required risk disclosures and questionnaire on knowledge, understanding risks and classification certification.

- In the "Understanding Risks" section of the account opening form, Mr S has ticked "Yes" to the statement that he understands high risk investments may also carry the risk that there is no guarantee of receiving the indicated returns.

As Mr S remained unhappy with the response he'd received from EGR, he referred the complaint to this service for an independent review.

One of our investigators issued an initial assessment upholding the complaint. In summary he said:

- There was insufficient evidence to say EGR advised, Mr S to invest, but he found it did carry out a regulated activity of arranging the investment.

- Mr S completed a HNW investor declaration, suggesting he did meet one of the categories of investor who could be promoted this type of investment. But this only covered part of the obligations on EGR when arranging investments of this type.

- EGR failed to meet its obligations with regards to ensuring the investments were appropriate for Mr S. The appropriateness test completed by EGR failed to adequately establish whether Mr S was knowledgeable and experienced in this type of investment and the risks it involved. And had it made basic enquiries around his circumstances, that ought to have led EGR to the reasonable conclusion that this bond wasn't appropriate for Mr S.

- Taking that into account, along with the information that EGR ought reasonably to have known about Mr S and its duty to act in his best interest, it shouldn't have allowed the application to go ahead. So, the investigator recommended EGR compensated Mr S due to its failings.

EGR didn't accept the investigator's opinion and asked for an ombudsman to reach a decision. In summary it said:

- It disputes the investigator's interpretation of its obligations under COBS 10 in relation to client knowledge and experience.

- In determining if EGR was in a position to be satisfied that Mr S had experience and knowledge to be able to understand the risks involved and generally whether the investment was appropriate, the evidence supports the finding that EGR was in such a position and was entitled to assess that the investment Mr S wanted to make was appropriate.

- It disagrees that the questionnaire completed by Mr S fell short of COBS 10 requirements and did not provide a basis for EGR to assess appropriateness. The questionnaire was part of a "*Preliminary Suitability & Assessment Test*" and the information contained in the document is also relevant. The document makes it very clear that the type of investment being considered is "*transactions in speculative illiquid securities*" and "*an instrument that is much riskier than a savings account*". Mr S also received the Information Memorandum (IM) which clearly explained the nature of the investment and its associated risks, including illiquidity. Mr S's answers to the questionnaire show his understanding of the risks.

- EGR is entitled to rely on what it was told by Mr S in terms of assessing if the investment was appropriate. Mr S informed EGR that he had previously invested in this type of product (illiquid securities) and had been involved in such investment for between 1 and 4 years, he had a high attitude to risk, he did not require access to the investment and he confirmed that he understood that this was a high risk and potentially illiquid investment. In the circumstances, EGR was entitled to come to the view that Mr S understood the risks involved with a very modest investment and that it was appropriate. So, EGR therefore fulfilled its requirements under COBS 10. Whether or not EGR knew the amounts or frequency of Mr S's similar transactions does not affect this assessment of appropriateness / understanding of risks, which, is a standalone test. If Mr S had only invested in a fixed rate savings account then he misled EGR and must bear responsibility for that.

- Even if Mr S was given a warning about the appropriateness of the investment, on balance, it would have made no difference to the outcome as the issues around the

high risk illiquid and unprotected nature of the investment had already been highlighted and had no impact on Mr S. So even if the opinion remains that the investment was not appropriate under COBS 10 and that EGR should have warned about this, there would have been no different outcome and therefore the complaint should still not be upheld – as Mr S would have proceeded regardless of a warning.

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.

What role did EGR play in the sale of the investment?

I've firstly considered EGR's involvement in the arrangements of Mr S's investment. It says it provided an execution only service and it didn't make a personal recommendation or assessment of suitability. I've considered the submissions EGR make on this point. I accept there isn't evidence of regulated advice being provided by EGR.

I've looked at the evidence available to show what EGR's involvement was. I've seen details of the application process. There is evidence of an application form provided by EGR that consisted of two stages, designed to meet the rules restricting who the bond could be promoted to and on how to test whether the investments were appropriate for the potential investor. The application form Mr S completed in April 2020 indicates he was categorised as a HNW investor. There was also an appropriateness test which asked questions about Mr S's knowledge and experience.

It's clear that EGR played an active and significant role in the arrangements of Mr S's investments. I am satisfied Mr S's complaint relates to a regulated activity. The bonds were a security or contractually based investment specified in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 ("RAO"). At the time Mr S made his investment, the RAO said regulated activities include arranging deals in investments. 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. So, I am satisfied the application process falls within the scope of Article 25(1). It involved making arrangements for Mr S to invest and had the direct effect of bringing about the transactions.

Did EGR meet its obligations to Mr S in the arrangement of the investments?

Mr S's complaint concerns what he considers to be a mis-sale of the investment. I'm satisfied that this includes EGR applying relevant tests regarding investor categorisation and appropriateness. Therefore, I will first set out the relevant considerations when looking at the application process EGR conducted before allowing Mr S to invest.

Relevant considerations

I have carefully taken account of the relevant considerations to decide what is fair and reasonable in the circumstances of this complaint. In considering what is fair and reasonable in all the circumstances of this complaint, I have taken into account relevant law and regulations; regulators rules, guidance and standards; codes of practice; and where appropriate, what I consider to have been good industry practice at the relevant time.

In my view the key consideration as to what is fair and reasonable in this case is whether EGR met its regulatory obligations when it carried out the acts the complaint is about. I consider the following regulatory obligations to be of particular relevance here.

The Principles for Businesses, which are set out in the FCA's Handbook "are a general statement of the fundamental obligations of firms under the regulatory system" (PRIN 1.1.2G). I think Principles 6 (Customers' interests) and 7 (Communications with clients) are relevant here.

Principle 7 overlaps with COBS 4.2.1R (1) (A firm must ensure that a communication or a financial promotion is fair, clear and not misleading), which I also consider to be relevant here.
I'm satisfied the investment Mr S applied for was a non-readily realisable security and therefore there were rules restricting who this type of product could be promoted to and how to test whether the investment was appropriate for the potential investor.

These rules were set out in COBS 4.7 and COBS 10. I have set out below what I consider to be the relevant rules, in the form they existed at the time.

COBS 4.7 - Direct offer financial promotions

COBS 4.7.7R said:

"(1) Unless permitted by COBS 4.7.8 R, a firm must not communicate or approve a direct offer financial promotion relating to a non-readily realisable security a P2P agreement or a P2P portfolio to or for communication to a retail client without the conditions in (2) and (3) being satisfied.

(2) The first condition is that the retail client recipient of the direct-offer financial promotion is one of the following:
(a) certified as a 'high net worth investor' in accordance with COBS 4.7.9 R;
(b) certified as a 'sophisticated investor' in accordance with COBS 4.7.9 R;
(c) self-certified as a 'sophisticated investor' in accordance with COBS 4.7.9 R; or
(d) certified as a 'restricted investor' in accordance with COBS 4.7.10 R.

(3) The second condition is that the firm itself or:
(a) the person who will arrange or deal in relation to the non-readily realisable security; or
(b) the person who will facilitate the retail client becoming a lender under a P2P agreement or a P2P portfolio,

will comply with the rules on appropriateness (see COBS 10 and COBS 10A) or equivalent requirements for any application or order that the firm or person is aware, or ought reasonably to be aware, is in response to the direct offer financial promotion."

COBS 10 – Appropriateness

At the time COBS 10.1.2 R said:

"This chapter applies to a firm which arranges or deals in relation to a non-readily realisable security, derivative or a warrant with or for a retail client, other than in the course of MiFID or equivalent third country business, or facilitates a retail client becoming a lender under a P2P agreement and the firm is aware, or ought reasonably to be aware, that the application or order is in response to a direct offer financial promotion."

COBS 10.2.1R said:

"(1) When providing a service to which this chapter applies, a firm must ask the client to provide information regarding his knowledge and experience in the investment

field relevant to the specific type of product or service offered or demanded so as to enable the firm to assess whether the service or product envisaged is appropriate for the client.
(2) When assessing appropriateness, a firm must determine whether the client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or service offered or demanded."

COBS 10.2.2R said:

"The information regarding a client's knowledge and experience in the investment field includes, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved, information on:
(1) the types of service, transaction and designated investment with which the client is familiar;
(2) the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;
(3) the level of education, profession or relevant former profession of the client"

COBS 10.2.6G said:

"Depending on the circumstances, a firm may be satisfied that the client's knowledge alone is sufficient for him to understand the risks involved in a product or service. Where reasonable, a firm may infer knowledge from experience."

COBS 10.3.1R said:

"(1) If a firm considers, on the basis of the information received to enable it to assess appropriateness, that the product or service is not appropriate to the client, the firm must warn the client."

COBS 10.3.2R said:

"(1) If the client elects not to provide the information to enable the firm to assess appropriateness, or if he provides insufficient information regarding his knowledge and experience, the firm must warn the client that such a decision will not allow the firm to determine whether the service or product envisaged is appropriate for him."

COBS 10.3.3G said:

"If a client asks a firm to go ahead with a transaction, despite being given a warning by the firm, it is for the firm to consider whether to do so having regard to the circumstances."

Having taken careful account of these relevant considerations, to decide what is fair and reasonable in the circumstances, and given careful consideration to all EGR has said, I'm satisfied the complaint should be upheld. I'll explain my findings below.

COBS 4.7 says that a firm must not communicate a direct or approve a direct offer financial promotion relating to a non-readily realisable security unless two conditions are satisfied.

The first condition is the client has been certified or has self-certified as one of the categories listed.

There is evidence that Mr S self-certified as a HNW investor – in that he signed a declaration in this respect. The wording used for the HNW category in the declaration signed by Mr S contains the wording set out in the rules – specifically elements that require to confirm the level of income and/or net assets held.

Mr S's application indicates that he held assets over £250,000. I haven't seen evidence to show what he held at the time from the point-of-sale information. In his complaint submissions he has suggested, from memory, his personal savings and investments were no more than £60,000 at the time.

Although not clear, it does seem possible that the declaration he made means he did meet one of the categories under COBS 4.7.7R - that being certified as a HNW investor. While I do have some reservations on this, it still possible the promotion could have been made to Mr S if he indeed did meet the criteria. But even if Mr S met the HNW criteria, this would only satisfy the first condition of COBS 4.7.7. I think EforG failed to satisfy the second condition – compliance with the rules relating to appropriateness under COBS 10.

The second condition set out in COBS 4.7.7R required EGR to comply with the rules on appropriateness, set out in COBS 10 and quoted earlier in my findings. The rules at the time (COBS 10.2.1R) required EGR to ask Mr S to provide information regarding his knowledge and experience – and for this information to be relevant to the product offered (the first limb of the rule). The rules required that information to then be assessed, to determine whether Mr S did have the necessary experience and knowledge in order to understand the risks involved (the second limb of the rule).

As set out above, COBS 10.2.2 R required EGR, when considering what information to ask for, to consider the nature of the service provided and the type of product (including its complexity and risks). It needed to think about asking questions on:

- the types of service, transaction and designated investment with which the client is familiar;

- the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;

- the level of education, profession or relevant former profession of the client.

Having reviewed the appropriateness test Mr S was directed to complete during his initial application in April 2020, I'm not persuaded EGR, asked for an appropriate amount of information about Mr S's knowledge and experience, as required by COBS 10.2.1R and COBS 10.2.2 R.

The questions asked were limited and the answers given by Mr S do not demonstrate the necessary experience and knowledge in order to understand the risks. Whilst I accept that, depending on the circumstances, a firm may be satisfied that the client's knowledge alone is sufficient for him to understand the risks involved in a product or service (COBS 10.2.6G), I'm not persuaded Mr S had the sufficient knowledge here.

I note he positively answered a question about whether he had made a similar investment in the past, but no detail is given about what this is despite the follow up questions asking for this detail. He also answered he had one to four years' experience of this type of investment – but again no detail is given of what this might refer to. In making his complaint, Mr S has told us his investment experience at the time was gained from investing in a building society bond with a guaranteed return. I haven't seen any other evidence that he held investments of the type he invested in through EGR prior to this. EGR say if Mr S had only invested in a

fixed rate savings account, then he misled EGR and must bear responsibility for that. But I don't think it is reasonable to draw this conclusion, where the evidence indicates the questions asked and the answers given don't suggest Mr S understood the relevance to why he was being asked. The fact his answers to key questions are incomplete also doesn't support he did have the knowledge and experience required. But I haven't seen EGR attempted to do anything further to satisfy itself of his knowledge and understanding. The relevant obligations are placed upon EGR, not Mr S.

EGR say based on the answers Mr S gave in his application, it was entitled to come to the view that he understood the risks involved and that the investment was appropriate for him. I don't agree this is sufficient to say it fulfilled its obligations under COBS 10. While EGR doesn't think it matters whether or not it knew the amounts or frequency of Mr S's similar transactions when assessing appropriateness, I disagree, the assessment completed doesn't, in my view, gather sufficient evidence for it to reach a decision to assess appropriateness.

Taking all of the evidence into account, I'm not persuade EGR did adequately test whether Mr S had the knowledge to understand the risk associated with the bond – I think this is particularly relevant for the initial transaction as this appears to be the first time he has invested in this type of complex investment. The evidence available all supports that his experience and level of knowledge was limited. The risks of the bonds were complex and multifactorial. It was not, for example, a question of whether Mr S simply understood money could be lost – but whether he was able to understand how likely that might be and what factors might lead to it happening.

As the first limb of COBS 10.2.1R was not met EGR was unable to carry out the assessment required under the second limb. EGR should have been confident, from the information it asked for, that it was able to assess if Mr S had the necessary experience and knowledge in order to understand the risks involved with investment in the bond. But it was not in a position to make such an assessment, based on the information it obtained. I accept that taking Mr S's appropriateness test answers in isolation would suggest he knew his capital would be at risk, But as mentioned, I've not seen that this would demonstrate an understanding of how likely it would be that he could lose his capital and/or what factors might lead to it happening.

Had EGR followed its obligations, I think the most likely conclusion it would have reached, was that Mr S did not have the necessary experience and knowledge to understand the risks involved with the bond.

If EGR assessed that the bond was not appropriate, COBS 10.3.1R said a warning must be given and the guidance at COBS 10.3.3G said a business could consider whether, in the circumstances, to go ahead with the transaction if the client wished to proceed, despite the warning. I've explained my concerns about the testing of Mr S's knowledge and experience, and had it adequately tested this, EGR would have come to the conclusion that the bond wasn't appropriate for him in the first place (so the later top ups would not be either).

A clear, emphatic statement would have left Mr S in no doubt the bond was not an appropriate investment for him. And he ought to have been privy to such a warning, had his appropriateness been tested in line with the requirements of the rules. Even if Mr S still said he wanted to proceed after being given a warning, I still think there is more EGR needed to do if it had asked for appropriate information about Mr S's knowledge and experience. In these circumstances, I think it would have been fair and reasonable for EGR to conclude it should not allow Mr S to proceed. Had Mr S been asked for appropriate information about his knowledge and experience this would have shown he may not have the capacity to fully understand the risk associated with the bonds. I've seen no evidence to show Mr S had

anything other than a basic knowledge of investments. So, it would not have been fair and reasonable for EGR, to conclude it should proceed if Mr S wanted to, despite a warning (which, as noted, was not in any event given).

In summary, I'm satisfied EGR did not act fairly and reasonably when assessing appropriateness. By assessing appropriateness in the way it did, it was not treating Mr S fairly or acting in his best interests. If it had acted fairly and reasonably to meet the relevant regulatory obligations when assessing appropriateness, Mr S would not have got beyond this stage.

I have noted the comments EGR make about the risk warnings contained in the Information Memorandum (IM). As the second condition set out in COBS 4.7.7R could not be met and things could not have proceeded beyond this, this means Mr S shouldn't have received the IM at all. And so, any information within that cannot now reasonably be relied on to show he was aware of the risks associated with the bond. I've also not seen sufficient evidence to show Mr S had the capacity to fully understand the IM – a lengthy and complex document – given his limited knowledge and experience. As such, EGR can't fairly rely on any possible reading of this as a means to correct the failings set out above.

EGR says during the application process Mr S was informed that capital is at risk, and full capital loss is possible and despite this evidence Mr S proceeded to invest in the bond regardless of what it did. However, I do not think it would be fair to say Mr S should not be compensated on this basis.

Firstly, Mr S should not have been able to proceed had EGR acted fairly and reasonably to meet its regulatory obligations. I acknowledge that other parties may have caused or contributed to Mr S's losses but, notwithstanding that, I'm satisfied it is fair to ask EGR to compensate Mr S as the appropriateness test was a critical stage, for which it was responsible for.

Secondly, for the reasons I have given, I am not in any event persuaded Mr S did proceed with a full understanding of the risks associated with the bond. I am not persuaded he looked at the full detail of the acknowledgements he gave, given what Mr S has said about his understanding of the bond and his lack of investment experience. I am not persuaded Mr S had the capacity to fully understand the risks associated with the bond – and he was in this position because EGR did not act fairly and reasonably to meet its regulatory obligations at the outset. I'm therefore satisfied it is fair to ask EGR to compensate Mr S for the losses he claims.

Putting things right

In assessing what would be fair compensation, I consider that my aim should be to put Mr S as close to the position he would probably now be in if he had not made his investments.

I take the view that Mr S 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 S' circumstances and objectives when he invested.

What must EGR do?

To compensate Mr S fairly, EGR must:

- Compare the performance of Mr S'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.

- EGR should also add any interest set out below to the compensation payable.
- Pay to Mr S £200 for the worry caused by the total loss of his investment.

Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Access Commercial Investors 4 Plc Bond	Still exists but illiquid	Average rate from fixed rate bonds	Date of investment	Date of my final decision	8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance)

Actual value

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

If at the end date any asset 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 S agrees to EGR taking ownership of the illiquid assets, if it wishes to. If it is not possible for Yes to take ownership, then it may request an undertaking from Mr S that he repays to EGR any amount he may receive from the portfolio 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.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, EGR should use the monthly average rate for one-year fixed-rate bonds as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

The two additional sums Mr S paid into the investment (after making the initial payment) should be added to the *fair value* calculation from the point in time when they were actually paid. This ensures all three contributions Mr S made are accounted for in the redress calculation.

Why is this remedy suitable?

I have decided on this method of compensation because:

- Mr S wanted to achieve a reasonable return without risking any of his capital.

- The average rate for the fixed rate bonds would be a fair measure given Mr S's circumstances and objectives. It does not mean that Mr S would have invested only in a fixed rate bond. It is the sort of investment return a consumer could have obtained with little risk to their capital.

My final decision

Your text here

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 21 November 2024.

Daniel Little
Ombudsman