summary of complaint

Mr R complains about investments he made through CSS Partners LLP (“CSSP”), an appointed representative of Charles Street Securities Europe LLP (“CSSE”).

Until 2008 CSSP was an appointed representative of CSS Inc, however CSSE Europe have taken responsibility for CSS Inc’s and CSSP’s actions. As Mr R’s complaint relates to a single financial service, I am satisfied that, in line with s234B FSMA, CSS Europe is the correct respondent firm in this case.

If I don’t consider further specification is required I’ll collectively refer to all CSS entities as “CSS” for ease of reading.

Mr R invested over £640,000 in shares of unlisted companies between 2006 and 2009. He says the recommendations CSS made were not in line with his stated objectives and were unsuitable for him.

background

Mr R became a client of CSS in 2006. He says he was led to believe CSS were handling shares in companies that were well known to them, had been thoroughly investigated and which they felt were sound companies that would soon be ready to be listed on the stock market. He was made to think the result would be a substantial increase in these companies’ share values which would be a good investment and would lead to capital growth which was Mr R’s investment objective.

Mr R says he agreed for CSS to advise him on high risk investments for only 20% of his portfolio. He says this was later changed to 25% on a form but he didn’t know why. He says he was given misleading advice on unsuitable shares which has led to at least 80% of his losses.

CSS describes its role as providing equity and debt finance for early stage growth companies. It invests as principal and raises money through private placements via its appointed representative CSSP.

Potential investors are contacted by CSSP and are asked to complete a “reply card” authorising CSSP to contact them to discuss their services. Interested investors would then complete a Private Client Agreement Form (“CAF”) which would allow CSSP to contact the investor at any time to discuss possible investment opportunities.

CSS says when companies approach them to raise finance they conduct due diligence checks and produce a memo with information about the company. CSSP would then contact the client and describe the investment opportunity. CSSP says no recommendations were given. They simply provided information about the companies Mr R could invest in and was for him to decide for himself whether the investment was right for him.

Mr R first signed a client agreement as a private client in January 2006. He then signed an agreement to be treated as an intermediate client a few months later in May 2006.

CSS raised several objections to our service considering Mr R’s complaint including it was brought outside the regulator’s time limits and that Mr R was an intermediate customer which meant this service didn’t have jurisdiction to consider his complaint.

I previously issued a jurisdiction decision in which I found the complaint had been made in time and that CSS didn't take reasonable care when they categorised him as an intermediate customer which meant he should have been treated as a private client. So I decided I could consider the merits of Mr R's complaint

I subsequently issued a provisional decision on the merits of Mr R's complaint. My provisional decision was to uphold Mr R's complaint. In summary I said:

- CSS gave Mr R advice and so they had to make sure the investments they recommended were suitable

- In CSS's client agreement, Mr R indicated that he was prepared to accept a high level of risk in respect of 25% of his investments. I considered that the sensible, objective construction to give to that term was that Mr R was prepared to accept a high level of risk in respect of 25% of the investments he made with or through CSS.

- This level of risk was breached straight away as all of CSS investments offered to Mr R were high risk. However, in my view Mr R understood the level of risk he was taking and the implications of it. I thought he made an informed choice to invest purely in high risk investments through CSS and over time was prepared to invest in more high-risk investments than he originally intended.

- Whilst I thought Mr R was prepared to take this risk, as part of the suitability assessment CSS was also required to consider whether Mr R had the required capacity for loss. I thought CSS should have stopped recommending high risk investments to Mr R when - based on the financial information they held for him-he was no longer able to reasonably bear the losses should those investments fail.

- Although the 25% term in the client agreement related to Mr R's preparedness to invest into high risk investments with CSS (which changed over time), I nonetheless thought 25% was a reasonable measure for CSS regarding Mr R's *capacity for loss* in the circumstances. I didn't think CSS could reasonably assume without further information from Mr R that his capacity for loss was than higher than this.

- CSS should have explained to Mr R when his investments reached 25% of his declared investment portfolio, that they considered he had reached a loss limit they thought he couldn't reasonably afford to exceed given his financial circumstances and that in turn they would not be recommending any more high-risk investments to him as it wasn't appropriate. If they had explained this, I didn't think Mr R would have insisted on continuing to invest in this way.

- Whilst Mr R was likely still interested in this type of investment, on balance I thought if CSS had raised the loss limit with him, he would have listened to CSS's concerns about the impact these investments could have on his financial situation and invested in lower risk investments. In any event I didn't think he would have invested to the same extent into high risk investments as he did with CSS.

- I intended to ask CSS to compensate Mr R in respect of all investments which had breached the 25% capacity for loss limit by comparing them to the value they would have had using a benchmark.

A copy of my provisional decision with my full reasoning is attached and forms part of this final decision.

Both parties were invited to provide further comments and information.

In response to my provisional decision Mr R, in summary, made the following comments:

- He made some speculative investments prior to dealing with CSS, but when he had to invest the proceeds of his share of the sale of the family business and of a property, he felt he needed to take a more responsible investment strategy. He thought CSS had the necessary expertise to safeguard his savings whilst giving him enough capital growth for his eventual retirement. This is why he only wanted 20% to be invested in high risk investments through CSS. He was encouraged to increase this figure to 25% which he reluctantly did. There was definitely never any question that this should have a bearing on any other investments or assets that he might have had.

- References made to his knowledge and experience are misleading. His professional experience was very different from the world of developing business, industry and manufacturing enterprises.

- He doesn't know where the sum of £750,000 that is mentioned in the decision comes from. He believes the sale of his family business produced in the region of £225,000 which was shared between him and his father and was made so his father could retire.

- If CSS had stopped recommending investments at any point, he would have sought the advice of a reputable established investment company. After his dealings with CSS, he put his pension funds into the hands of St James Place and Fisher Investments, both highly reputable investment management companies.

- He would be pleased to return full ownership of the shares to CSS. He believes all his CSS holdings have a near negligible resale value. He is worried that CSS will have a creative and biased view on the valuation of his shareholdings and queries whether third-party valuations can be carried out.

CSS, through their representatives, disagreed with my decision. In summary they said the following:

- CSS considers they have been treated unfairly and have not been given sufficient time and opportunity to provide submissions. They say Mr R had been given two years to reformulate his complaint after a previous ombudsman decision was quashed by consent in January 2019. However, they had only been given three and a half weeks to respond to my provisional decision on the merits of Mr R's complaint which they find unreasonable. They had been presented with a fait accompli in respect of each decision that was issued. They said they would challenge the jurisdiction decision.

With regards to the merits, CSS said:

- The ombudsman imposed obligations on CSS that were unreasonably onerous. In concluding that CSS had a duty to decide the level of risk that Mr R could take (contrary to Mr R's own wishes) and to deny him access to such investments beyond that level, impose a duty on CSS which goes far beyond that of an investment adviser. A distinction is drawn between subjective and emotive attitude to risk and objective capacity for loss. The distinction is unsupported by evidence and unjustifiable. An adviser or information provider has no business preventing its client from accessing potential investments, let alone a duty to do so.

- The ombudsman's calculation of Mr R's objective capacity for loss is arbitrary and erroneous. She concluded that the capacity for loss is intrinsically linked to the 25% limit on high risk investments. However, if Mr R knew, as the ombudsman concluded, that all of the CSS investments recommended to him were high risk, then Mr R can't also have maintained a 25% risk threshold in relation to the same investments throughout the relationship with CSS.

- In any event the ombudsman has miscalculated the capacity for loss against Mr R's portfolio. She has failed without proper justification, to include the sale of Mr R's business for £750,000 in the calculation of Mr R's total portfolio. This asset was included for the deal on 10 September 2007. The ombudsman has not explained why CSS should have disbelieved Mr R when he informed them of the sale.

- The calculation based on capacity for loss against total portfolio would also have to allow for EIS income tax and loss relief. The ombudsman has not included this in her calculations.

- Without a full and frank disclosure of Mr R's actual value of his portfolio at the relevant times, the ombudsman cannot be in a position to say whether a 25% capacity for loss was in fact exceeded.

- The decision fails to take into account that Mr R was in a better position to judge his capacity for loss. CSS points to the wide range of investment sizes throughout his dealings with CSS indicating he was being selective on the type and size of investments he wished to make.

- One of Mr R's investment statements he provided from 2002 showed a net loss to his portfolio of 49.4% (£52,294). This evidences a willingness to exceed a 25% capacity for loss. If he had told this investment company he had £150,000 in assets (as he had with CSS), this would have represented a loss against these assets of 35%.

- CSS reiterated that Mr R had continued to invest in two private companies in 2012 and 2015, both of which are now in liquidation. CSS expects these are just two of many investments like this.

- CSS questions Mr R' transparency in providing information to this Service. There is no evidence to support Mr R's suggestions that he *"initially must have been under the impression that the shares were normal type of shares that I was familiar with in small developing companies with some sort of track* record.*"* And Mr R allowed this Service to draw the conclusion that a client form dated 30 September had been provided to CSS which they assume he relied on to suggest that he was only interested in FTSE 100, FTSE 250 and 350 and Small Cap Index. CSS also identified a further non-listed investment Mr R made prior to becoming a CSS client. They provided evidence he invested in Biocide International PLC in July and August 2005 which was EIS qualifying. CSS say this is further evidence Mr R has attempted to mislead this service in relation to his experience in non-listed companies.

- Given Mr R's prior and subsequent investment experience and his lack of transparency about this, CSS considers the ombudsman cannot make a fair decision without requiring Mr R to disclose all investments made after his relationship with CSS concluded. Without this, the ombudsman is speculating what Mr R would or wouldn't have done, when in fact the emerging picture from CSS's research is that he would have continued to invest above a 25% capacity for loss.

- There's no evidence cited or relied upon in the decision that any alternative investments Mr R would have made instead of CSS's investments wouldn't have been high-risk.

- There's an inconsistency between the ombudsman's findings that the 25% high-risk investments limit was against investments through CSS and yet the 25% capacity for loss is measured against Mr R's total portfolio.

- CSS has no duty to compensate Mr R for investment losses. Mr R took the decision to enter into high risk intermediate investments in respect of which he suffered loss. CSS does not as a matter of law assume responsibility for the decision to enter the transaction. CSS is only liable for the consequences of the information he was given being wrong or failure to give him the wrong information.

- To identify the extent of any duty on CSS to compensate Mr R, it is necessary to consider whether Mr R would have incurred the losses if he had entered into the high risk investments had CSS told him that that high risk investments formed more than 25% of the investments he had with him. It is self-evident in the present case that he would have suffered precisely the same losses. In those circumstances, CSS can be under no duty to compensate him for them.

- The purpose of the COB is to protect the client from a failure to understand the risk of market movement in value of the type of investment proposed. However, Mr R knew the investments he was committing to were high risk and that their value could be lost.

- The complaint should therefore not be upheld in circumstances where the loss suffered by Mr R is properly attributable to: (i) the misrepresentations which he made to CSSE in order to induce CSSE to categorise him as an intermediate investor and, thereby, to obtain access to access to high risk intermediate investments; (ii) Mr R's decision to enter into them in the knowledge that they were high risk investments; and/or (iii) the market movement in respect of the said investments.

my findings

I've re-considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

I've considered Mr R's response to my provisional decision and note that despite Mr R repeating he only wanted 20-25% of his investments with CSS to be high risk and that he wanted his investments to be secure, I'm still satisfied that Mr R had sufficient experience and knowledge to understand what sort of investment opportunities CSS was recommending to him and that these were all high-risk investments into unlisted companies. It follows that although the objective, sensible interpretation of the contractual agreement at the outset of the relationship between Mr R and CSS was that Mr R wanted only 25% of the investments arranged through CSS to be high risk, as the relationship unfolded it seems clear that Mr R was prepared to invest completely into high risk investments through them.

I don't find it plausible that he considered the investments he was making were safe and secure investments. He might not have had direct experience in all of the trading sectors of the businesses he was investing in. However, I think he knew a reasonable amount about how the stock market worked and about the unexpected difficulties small businesses could encounter and could therefore understand that these businesses could fail to achieve what they intended to. And considering the risk warnings in the diary notes and the placement information he was sent by CSS, I think he would have understood these were non-standard, high risk investments. I remain of the view that notwithstanding what was agreed in the client agreement at the outset of the relationship, Mr R understood that the investments proposed to him by CSS over time were all high risk.

I now turn to CSS's comments.

Procedural fairness

I would like to clarify that Mr R was not invited to 're-submit' or 'reformulate' his complaint after a previous ombudsman's decision was quashed in January 2019. The consent order and correspondence at the time said his complaint would be remitted for reconsideration by a new ombudsman and this is what happened. Mr R did send another summary of his complaint but it didn't contain any materially new information. Unfortunately, following the quashing of the decision, Mr R's complaint was waiting to be re-allocated to a new ombudsman for some time.

I issued a provisional jurisdiction decision on 24 February 2021 based on the information that had been submitted by Mr R and CSS. CSS asked for more time to reply because they wanted to request legal advice and they were given a total of two months to respond. Subsequently, a jurisdiction decision was issued on 12 February 2021 which considered submissions by both parties. I concluded that this service had jurisdiction to consider Mr R's complaint and that I would start considering its merits. As the merits had been considered previously by the first ombudsman (whose decision was quashed), very detailed submissions from CSS and Mr R were already on file and CSS had made no indication that they had any additional submissions to make. On that basis, I considered the evidence available and issued my provisional merits decision. I made it clear the decision on merits was provisional, which allowed both parties further opportunity to comment. Both parties were given two weeks to reply. CSS asked for an additional three weeks response time. They were informed that without specific reasons why several more weeks were required, an extension of another one and half weeks would be granted. CSS provided no further reasoning as to why they needed more time beyond this and provided their response within the given deadline.

Overall, I'm satisfied both parties were given equal and reasonable time and opportunity to make submissions and comments at any stage of the process which has been going on over several years.

CSS say they will challenge the jurisdiction decision. However, I note that they didn't submit any further comments after the jurisdiction decision was issued or in their most recent submissions about why they disagree with the findings I made.

CSS's comments on the merits of Mr R's complaint

I don't agree that I imposed unreasonable obligations on CSS. As I explained in my provisional decision, I consider CSS gave Mr R investment advice and was not merely promoting and arranging the investments he eventually purchased. In turn CSS had to do more than just ensure the information they gave Mr R was correct, as they have suggested. They had to make sure their investment recommendations were suitable. In order to give a suitable investment recommendation, CSS needed to go further than to simply take account of Mr R's preferences and understanding regarding risk. CSS also needed to ensure that the investments were suitable for Mr R, taking his wider financial position into account. It is my view that this obligation has always been a feature of good industry practice in the giving of suitable investment advice and was made explicit by the FCA in its Conduct of Business Sourcebook (COBS 9.2.2R):

COBS9.2.2R

(1) A firm must obtain from the client such information as is necessary for the firm to understand the essential facts about him and have a reasonable basis for believing, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of managing:

(a) meets his investment objectives;
(b) ***is such that he is able financially to bear any related investment risks consistent with his investment objectives;*** *and*
(c) is such that he has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio. [My emphasis.]

CSS was also, of course, required to comply with the FCA's Principles for Businesses and in turn was obliged to conduct its investment business with Mr R in a manner that paid due regard to his interests and to treat him fairly.

I have taken all of this into account when forming my views of the fair and reasonable outcome in this case. I maintain that it was unreasonable for CSS to continue to propose high risk deals to Mr R after the point at which it became reasonably clear, based on the information they had, that he was no longer financially able to bear those losses.
In saying that, I have noted the particular manner of dealing between Mr R and CSS. Mr R was not simply receiving advice from CSS in connection with a single investment proposition. Instead, there was an ongoing advisory relationship between the two, with CSS phoning Mr R sometimes multiple times a month over the course of several years in order to recommend various investment options. As things transpired, I understand very few of them ever resulted in any investment returns for Mr R and he hasn't been able to access his capital of over £600,000. In my view, it was unreasonable for CSS to continue to call Mr R with further high-risk investment propositions after the point at which he could no longer reasonably absorb any further losses. An investment that exceeds a client's capacity for loss shouldn't be recommended, even if the client is willing to take that risk. CSS wasn't simply an "order taker" in these circumstances. They had to take reasonable steps to make sure the investments recommended to Mr R were suitable for him and to act in his best interests.

CSS says that the threshold figure I have used (25% of his total portfolio) to mark the point at which Mr R could no longer absorb these investment losses is inconsistent with my findings on the '25% term' in the client agreement. As explained, I think the sensible, objective construction of the client agreement is that the 25% term related only to CSS investments. It was simply a statement from Mr R at the outset of the relationship about the level of higher risk investments he was willing to purchase with or through CSS.

However, the capacity for risk analysis is entirely distinct from this. In order for CSS to assess to what extent Mr R could bear any losses from his CSS investments, they needed to know what other financial assets he had that he could fall back on. Having as much information about the financial and personal circumstances of a client is essential to assess suitability of an investment, including someone's capacity for loss.

I want to be clear that I consider the 25% term in Mr R's client agreement only related to his willingness to take high risk at the outset of the relationship, i.e. his attitude to risk in relation to his CSS investments. That is a subjective decision on his part and it could change, at any point – which, as I've already outlined, is what I think happened as the advisory relationship unfolded. The analysis of a person's capacity for loss, on the other hand, is a measurable and objective fact, which should be undertaken regardless of what the customer thinks or feels about investment risk.

CSS has said that 25% is an arbitrary and erroneous figure. I want to assure CSS that I have given this figure careful thought. It is true that the regulator is not prescriptive about the point at which a person's capacity for loss should be capped. Instead, it is a matter for the advising firm to assess on a case by case basis, giving full account to the information the firm has obtained from the client about his objectives and his financial and personal circumstances. As CSS itself acknowledges, it did not have adequate information about Mr R's financial circumstances. CSS didn't complete a proper fact find and important information about Mr R's circumstances, such as his income and expenditure, was never considered. In those circumstances, CSS says that Mr R was in a better position to judge his capacity for loss as he would have known what assets and other investments he had.

However, and as CSS will appreciate, the obligation to assess Mr R's capacity for loss fell to CSS and it was for them to make sure they had obtained adequate information from Mr R in order to make that assessment (COB 5.2.5R and COBS 9.2.1R(2)). To the extent that they considered there were deficiencies in the information they had, it was for them to ask Mr R further questions at the time to put things straight.

In the absence of that further information, it is still my view that CSS should nonetheless have seen from the information they did have that there was a point at which Mr R could no longer afford to absorb the potential significant investment losses he could incur. As I said in my provisional decision, CSS recorded on their existing client and suitability reports the value of Mr R's overall portfolio each time Mr R made an investment. I consider that CSS should reasonably have used this to assess his capacity for loss on an ongoing basis. I also think CSS acknowledged that this was something they should have considered. In an email to us in November 2016 CSS said:

*Mr R did inform the firm in 2006 that he had sold his business for some £750,000, which reassured us that the **quantum of money** he was investing in the opportunities we were presenting **was appropriate to his circumstances.** [my emphasis].*

I appreciate CSS thinks I should make enquiries of Mr R to determine what his actual portfolio values were during the advisory period. However, I think it's difficult now to establish with sufficient certainty Mr R's financial position from 15 years ago. So in the circumstances I remain satisfied that it's fair to take account of the reasonable assumptions CSS should have made about Mr R's capacity for loss based on the information they did have.

I felt 25% of his total portfolio was a reasonable starting point for CSS, particularly as they told us in their letter of 29 January 2018 that the 25% limit was guidance from Mr R as to

'*how much exposure he wanted to take at that time and* ***therefore, broadly, how many investments we should offer to him.*** *[CSS's emphasis]. CSS always kept that broad limit in mind when offering new prospects, but it was always [Mr R's] sole decision whether to invest in new companies, even in circumstances where we offered him opportunities such that he was close to the 25% figure.*

…

'the 25% figure was general guidance to CSSP as to which investments CSSP should introduce to [Mr R] and that, based on the information we had at the time, the percentage held in private companies did not exceed the guidance level of 25% of total portfolio.'

Given Mr R's age and that he had told CSS on his client form he was retired, they should have considered that losing any more than a quarter of his investment portfolio would likely start to have a material impact on his standard of living and, in particular, his ability to enhance his benefits in retirement. As I said in my provisional decision, the investments Mr R was entering into were not just high risk to the point where they could fluctuate, lose value or take some time to come to fruition. There was a genuine risk that Mr R could lose all of the capital he was investing. Holding 25% of a total investment portfolio in such assets is already high in my opinion and I would say many investors would not have the capacity to even lose this much. However, Mr R hadn't refuted at any point that 20-25% of his overall portfolio was a reasonable assumption for his capacity for loss. So in the circumstances I still think it is reasonable to assume that Mr R had a capacity for loss of 25% of the portfolio value he declared to CSS. I don't think CSS could reasonably assume without further information that his capacity for loss was higher than this.

In saying this, I note also that CSS' current submission that a capacity for loss requirement of 25% of Mr R's general investment portfolio is erroneous and arbitrary appears to contradict their earlier stance on the meaning of the 25% term in the client agreement. In opposition to my finding that the 25% term was a reference to the investments made *through CSS*, the firm has consistently said that it was in their view a reference to Mr R's *wider investment portfolio*, as disclosed in the agreement. It seems CSS is happy to say that it had contractually agreed to keep Mr R's investments at a level that did not exceed 25% of his overall investment portfolio, but at the same time say that same obligation would be too onerous if it were applied as part of the suitability assessment itself. I'm afraid I find CSS' arguments in this regard to be inconsistent and unhelpful.

CSS says Mr R's previous investment statements from 2002 with a different investment company show losses to his portfolio of 49.4 % and that this showed Mr R's willingness to exceed a 25% capacity for loss. However, as CSS surely is aware, an investment statement is a snapshot of how an investment is performing. Unless Mr R realised his investments at this point (and there's no evidence he did), he didn't in fact suffer any losses. It's normal for an investment portfolio to fluctuate and contrary to the CSS investments, Mr R's holdings with this company were mostly in listed companies and far less likely to lead to complete losses over the medium to longterm. I don’t think this is either conclusive evidence that Mr R had a higher capacity for loss nor that he was prepared to exceed his objective capacity for loss limit, no matter what an adviser was telling him.

As outlined above, I also disagree with CSS that they are not required to compensate Mr R for his investment losses and that they are only liable for consequences caused by any wrong information they gave Mr R. As I say, because CSS gave investment advice to Mr R, their obligation here was more than just to give correct information to him. They had to give suitable advice.

I acknowledge that Mr R did make a choice to make high risk investments and I agree that he understood that their value could be lost. For that reason, I decided his attitude to risk had shifted from the stance he had indicated at the outset by way of the 25% term in the client agreement. CSS have pointed to another EIS investment (Biocide International Plc) Mr R made in 2005 before he became a CSS client and have questioned how transparent Mr R has been about the information he provided to this service. They say this is further evidence he had previous experience in EIS investments when he said he didn’t.

I have taken all of this information into consideration and as already explained in my provisional decision, I think Mr R had a higher attitude to risk and more experience than his submissions to us have intimated. And that is precisely why I don’t hold CSS responsible for all of Mr R’s losses even though I consider CSS should have told him he was exceeding the 25% term in his client agreement early on in their relationship. That is because, in my view, even if they had done so, it is more likely than not that Mr R would have been prepared to exceed his initially chosen limit and agreed to continue with the high-risk CSS investments. I say this because in my opinion he came to understand that all the investments he made through CSS were high risk.

However, I think the matter would have been different if CSS had clearly told him at the appropriate point that he had reached the limit of his capacity for loss. As explained in my provisional decision, CSS should have explained to Mr R that in their view the amount he had invested in high risk investments had reached a loss limit they thought he couldn’t reasonably afford to exceed given his financial circumstances, and that in turn they would not be recommending any more high-risk investments to him as it wasn’t appropriate. If they had explained this, I don’t think Mr R would have insisted on continuing to invest in this way.

In saying this, I note that Mr R has said throughout his complaint that he was looking for professional advice and support when making investments, so I don’t think he would have simply ignored any clearly communicated concerns of his adviser. From what I’ve seen it looks like CSS was generally initiating contact by way of frequent calls from Mr R’s client adviser. It follows that if they had told him they would stop calling him to make recommendations, I think it’s more likely than not he wouldn’t have actively pursued high risk investments through them or through any other financial adviser. Consequently he wouldn’t have ended up with investments through CSS which breached that limit.

I think this is what would likely have happened if CSS had followed their regulatory obligations and good industry practice at the time. But it is also, in any event, my view of the fair and reasonable outcome in all the circumstances of the case. If CSS had acted in Mr R’s best interest by informing him of their concerns about his ability to absorb potential losses at this monetary level and stopped recommending high risk investments, I am satisfied Mr R wouldn’t have made any further investments exceeding his capacity for loss limit through CSS.

It's reasonable to assume Mr R would have invested his money elsewhere. I considered whether he would have invested his money in the same type of high-risk investments with a different firm. However, I don't think it's reasonable to assume he would have done this if he had just been warned by CSS that the loss from high risk investments was starting to damage his wider financial position and that as a result, further investment of this kind wasn't in his best interest. And even if he did approach another adviser for advice on high risk investments, I think he would have found it difficult to find another firm that was reasonably prepared to deal with him exclusively in similar types of high-risk investments at this point given his existing exposure to these investments.

This isn't to say Mr R would have invested in particularly low risk investments instead. As explained previously, I think he likely had a medium to high attitude to risk overall, so alternative investments would likely have included some higher risk investments. That is why my redress formula directs CSS to use a benchmark that takes this spread of investments into account. Mr R says he would have approached an established investment company if CSS had stopped calling him with investment recommendations. This doesn't sound implausible to me, given that he had invested with companies like Barclays and Hargreaves Lansdown before.

I have also now asked Mr R to provide information about the investments he actually purchased after his dealings with CSS finished. I can see from that information that he went on to invest in in portfolios with Fisher Investments and St James Place from 2010/2011. The statements provided, which were more recent, show Mr R being invested mainly in UK and global equities with a smaller amount invested in cash and property which indicates a spread of medium to high risk investments. As I have said, it is difficult now to get an accurate picture of what happened many years ago when Mr R's relationship with CSS ended. I should stress that the information Mr R has now given me does not, of itself, inform my decision making on the causation issue here. I acknowledge that the information gives an indication how Mr R invested his money years after his relationship with CSS ended and after he had sustained considerable loss. It is therefore not determinative of how Mr R might have invested if CSS had told him earlier on in the relationship that he was exceeding his capacity for loss. In answer to that question, I have had to make certain assumptions about what Mr R would likely have done. Nonetheless, I note that the information does not contradict the assumptions I have made and supports my view that Mr R likely had, more generally, a medium to high risk attitude to investment risk.

I appreciate that CSS provided evidence of Mr R investing in two private companies in 2012 and 2015 which have both gone into liquidation since. And Mr R admitted that he has had the occasional "dabble" in smaller companies with some money he was prepared to lose, but never with his serious pension investments. Whilst this shows Mr R was still interested in this type of high-risk investment a few years later, I don't think it's sufficient evidence to show that he would have invested all his money in this type of investment no matter what CSS had told him about his capacity for loss.

Overall, it's impossible to say what exactly Mr R would have invested in 15 years ago if CSS had raised concerns about his capacity for loss. And I appreciate using a benchmark can never be perfect. However, I remain satisfied the benchmark used is reasonable in the circumstances.

CSS say I didn't include Mr R's business sale value in the calculations without proper justification. I disagree. In my provisional decision, I explained that I couldn't see what information they were actually given about the business sale by Mr R and at what point. The diary notes in January 2006 show that Mr R was in the process of selling his business and it looks like this sum was mentioned; but in March 2006 the notes record that he sold his business for over £100k and a couple of weeks later it's noted the sale fell through. I haven't seen any other evidence to show what information Mr R had given CSS about the sale of his business after that.

The proceeds of the sale also weren't specifically considered in the portfolio size when CSS completed their records before each investment. There is no mention of it. CSS says it was recorded as an asset for Mr R's investment on 10 September 2007, however neither the diary notes around this time nor the corresponding existing client and suitability report for this investment mentions this.

CSS has not provided any further evidence about this, so I can't see on what basis CSS is able to say that Mr R told them the business was sold for £750,000. Any increases in the recorded portfolio value which weren't down to CSS investments could have in theory also been funded from the sale of his business, for example the increase in savings, tradeable assets or the higher value of a second property which was recorded by CSS. So I don't think CSS could have considered this sum in addition to the portfolio values when assessing Mr R's exposure to high risk investments, without clearer information from Mr R about the business sale. Mr R says he believes he sold his business for around £225k and split this with his father. I appreciate it's possible Mr R told CSS he would receive a higher value at some point and if he had done so, I think CSS could have relied on this. However, I've seen no evidence that this is what happened here.

CSS said EIS income tax relief and loss relief should be allowed for in my redress calculations. I think they have a valid point here. I understand that in 2006 Mr R would have been entitled to 20% income tax relief on any EIS investment. I have asked Mr R for information about this. He said he could only find one EIS registration form for Urban Wimax for an investment of £20,000 and he did claim for tax relief on this. He can't recall receiving any other forms, but if he did he would have passed them on to his accountant to use with his tax return.

I think it's reasonable to assume Mr R was able to claim back 20% of the investment value immediately through income tax relief, so I think it's fair to say he was in effect only using 80% of capital for his EIS investments (Urban Wimax, Safe and Morria). For the purposes of calculating the capacity for loss limit I think it's reasonable in the circumstances for CSS to reduce the original investment amount for his EIS investments by 20%. I've allowed for this in the redress table below.

Mr R might also have been able to claim loss relief on these investments. I have taken account of the fact that loss relief would have only been available to him at some point in the future and only in certain circumstances. For example he had to keep the shares for a certain number of years, the company had to keep their qualifying status and it would only be paid if Mr R disposed of the shares. Before any potential loss relief might have been paid to Mr R, he likely could have faced illiquidity issues and be stuck with these shares in the meantime, so I don't think any such relief should fairly be taken off his initial investment for these capacity for loss calculations.

However, if Mr R did dispose of his EIS investments at any point or the relevant company went into liquidation and Mr R was eligible for loss relief at this point, then CSS can deduct these amounts from the fair value together with any other withdrawals, income payments etc.

I've considered that it's possible that Mr R didn't claim income tax or loss relief on his EIS investments even though he was entitled to. However, I think on balance it's reasonable to assume that he would have claimed when he could and in any event, to mitigate losses, I think he should have done so. So in turn it's fair that CSS can make these deductions if applicable.

Having reviewed all information and submissions by the parties again, I still consider it fair and reasonable that Mr R's complaint should be upheld.

fair compensation

In assessing what would be fair compensation, I consider that my aim should be to put Mr R as close to the position he would probably now be in if he had not been given unsuitable advice.

I think any funds he wouldn't have invested through CSS (at the point they breached his capacity for loss) would still have been invested but would have been invested differently by Mr R. I don't know exactly what he would have invested in instead. However, and in line with my assessment of his broader portfolio risk profile, I am satisfied that what I have set out below is fair and reasonable taking that into account and given Mr R's circumstances and objectives when he invested.

how should the 25% capacity for loss limit be assessed?

I think it's reasonable in the circumstances to consider that CSS should have based their assessment whether Mr R had the capacity for loss on the financial information they had recorded about Mr R's investment portfolio. I appreciate CSS says Mr R's investment portfolio might have had a much higher value, for example they referred to a commercial property he held in his self-invested personal pension that they weren't aware of at the time. And given what Mr R said to this service about being modest in his declarations to CSS, this is quite likely. The argument here would be that a higher portfolio value would mean a higher capacity for loss in monetary terms.

But I think CSS could only consider suitability based on the information available to them. If they considered the information to be inadequate, it was for them to ask Mr R further questions at the time. I do not think it is reasonable now, many years down the track, to try to get a clear picture of Mr R's financial circumstances at the time. The analysis should be based on the full extent of the information CSS had obtained from Mr R at the time. There is of course a possibility that that information underestimated Mr R's wider financial position. But equally, if Mr R had overstated his assets at the time, I would expect CSS to be able to rely on the information Mr R had provided.

The value of Mr R's investments that was known to CSS changed over time. In January 2006 Mr R said he had £100k in tradeable investments and £50k in liquid savings. Over time the value increased. Whenever an investment was made CSS recorded Mr R's portfolio size and the information they held was regularly verified with Mr R. I've seen financial information reports which were sent to him and which he amended where he saw necessary, so I think it's reasonable to rely on these values.

On 9 July 2009, when making his last investment through CSS, his portfolio size was recorded as £1.735,710.85 which was broken down as:

Tradeable investments: £135,750
Liquid savings: £70,000
Peps ISAs: £150,000
Private/unquoted companies: £639,960
2nd property: £740,000

These values included all of the CSS investments including the one he was about to make. As explained above no additional sum for Mr R's business sale should be added here.

I think it would have been clear to Mr R that CSS weren't providing advice on his overall financial situation and could only consider information they had. He was advised by CSS to provide as much information about his financial situation as possible and I think in these circumstances it's reasonable for CSS to only consider the information they were provided by Mr R and apply his capacity for loss limits to these values.

Before recommending an investment, I think CSS should have referred to the current portfolio size on their existing client and suitability report (amount set out under *'Total'*) and worked out whether this next investment would take Mr R's CSS portfolio above his 25% capacity for loss.

Using these numbers on the CSS reports and the investments Mr R made, with allowances for EIS income tax relief, (see table below), I consider that the last suitable investment recommended to Mr R was the *Miras* investment on 20 September 2006 for £11,250. <u>Every investment after this date exceeded Mr R's 25% capacity for loss limit, so was an unsuitable investment that shouldn't have been recommended</u>. It follows the unsuitable investment amount is £403,902.66.

what should CSS do?

To compensate Mr R fairly, CSS must:

1) compare the performance of Mr R's unsuitable investments with that of the benchmark shown below and pay the difference between the fair value and the actual value of the investments. If the combined actual value is greater than the combined fair value, no compensation is payable. CSS should also pay interest as set out below. Income tax may be payable on any interest awarded.

investment name	benchmark	from ("start date")	to ("end date")	additional interest
Unsuitable investments in CSS portfolio (as identified above)	FTSE UK Private Investors Income Total Return Index	date when each unsuitable investment was made	date of my final decision	8% simple per year from date of decision to date of settlement (if compensation is not paid within 28 days of the business being notified of acceptance)

Actual value

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

If at the end date an investment 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 R agrees to CSS taking ownership of the investment, if it wishes to. If it is not possible for CSS to take ownership, then it may request an undertaking from Mr R that he repays to CSS any amount he may receive from the investment 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.

Any withdrawal, income or other payment out of the investment (including any EIS loss relief) 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 are a large number of regular payments, to keep calculations simpler, I will accept if CSS totals all those payments and deducts that figure at the end instead of deducting periodically.

why is this remedy suitable?

I have chosen this method of compensation because:

- Mr R wanted capital growth from the investments he purchased through CSS and was willing to accept high investment risk in connection with those investments.
- However, CSS should not have recommended investments that exceeded Mr R's threshold for capacity for loss of 25% of his wider financial portfolio that was known to CSS.
- If CSS had explained that threshold for loss to Mr R and stopped recommending high risk investments, Mr R would likely not have invested the level of money he did in high risk investments of the same type through CSS or elsewhere.
- He would still have invested the money that exceeded his 25% threshold for loss and any alternative investments would likely still have a reasonable amount of 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 R's circumstances and risk attitude.

I appreciate CSS think this benchmark doesn't reflect sufficiently that Mr R was likely to continue in high risk investments be it through CSS or elsewhere. However, and as I've outlined above, I'm satisfied that on balance and following the explanation of his capacity for loss, Mr R would not have invested all sums he didn't invest through CSS into the same category of high-risk investments elsewhere. So I think on balance the index used is reasonable in these circumstances.

my final decision

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £150,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £150,000, I may recommend that CSS pays the balance.

Determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My final decision is that CSS should pay the amount produced by that calculation up to the maximum of £150,000 plus any interest set out above.

Recommendation: If the amount produced by the calculation of fair compensation exceeds £150,000, I recommend that CSS pays Mr R the balance plus any interest on the balance as set out above.

If CSS does not pay the full fair compensation (including the recommendation if fair compensation exceeds £150,000), then any investment currently illiquid should be retained by Mr R. This is until any future benefit that he may receive from the investment together with the compensation paid by CSS (excluding any interest) equates to the full fair compensation as set out above.

CSS may request an undertaking from Mr R that either he repays to CSS any amount Mr R may receive from the investment thereafter or if possible, transfers the investment at that point.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr R to accept or reject my decision before 27 April 20212.

Nina Walter
ombudsman

<u>copy of my provisional decision</u>

summary of complaint

Mr R complains about investments he made through CSS Partners LLP ("CSSP"), an appointed representative of Charles Street Securities Europe LLP ("CSSE").

Until 2008 CSSP was an appointed representative of CSS Inc, however CSSE Europe have taken responsibility for CSS Inc's and CSSP's actions. As Mr R's complaint relates to a single financial service, I am satisfied that, in line with s234B FSMA, CSS Europe is the correct respondent firm in this case.

If I don't consider further specification is required I'll collectively refer to all CSS entities as "CSS" for ease of reading.

Mr R invested over £640,000 in shares of unlisted companies between 2006 and 2009. He says the recommendations CSS made were not in line with his stated objectives and were unsuitable for him.

background

Mr R became a client of CSS in 2006. He says he was led to believe CSS were handling shares in companies that were well known to them, had been thoroughly investigated and which they felt were sound companies that would soon be ready to be listed on the stock market. He was made to think the result would be a substantial increase in these companies' share values which would be a good investment and would lead to capital growth which was Mr R's investment objective.

Mr R says he agreed for CSS to advise him on high risk investments for only 20% of his portfolio. He says this was later changed to 25% on a form but he didn't know why. He says he was given misleading advice on unsuitable shares which has led to at least 80% of his losses.

CSS describes its role as providing equity and debt finance for early stage growth companies. It invests as principal and raises money through private placements via its appointed representative CSSP.

Potential investors are contacted by CSSP and are asked to complete a "reply card" authorising CSSP to contact them to discuss their services. Interested investors would then complete a Private Client Agreement Form ("CAF") which would allow CSSP to contact the investor at any time to discuss possible investment opportunities.

CSS says when companies approach them to raise finance they conduct due diligence checks and produce a memo with information about the company. CSSP would then contact the client and describe the investment opportunity. CSSP says no recommendations were given. They simply provided information about the companies Mr R could invest in and was for him to decide for himself whether the investment was right for him.

Mr R first signed a client agreement as a private client in January 2006. He then signed an agreement to be treated as an intermediate client a few months later in May 2006.

CSS raised several objections to our service considering Mr R's complaint including it was brought outside the regulator's time limits and that Mr R was an intermediate customer which meant this service didn't have jurisdiction to consider his complaint.

I previously issued a jurisdiction decision in which I found the complaint had been made in time and that CSS didn't take reasonable care when they categorised him as an intermediate customer which meant he should have been treated as a private client. So I decided I could consider the merits of Mr R's complaint which I'll do in this decision.

my provisional findings

was Mr R given advice?

CSS says they only provided information to Mr R and it was up to him to decide if he wanted to proceed and if it was right for him and his circumstances. Mr R says he was given recommendations and advice. So I have first considered whether CSS gave advice to Mr R.

During the time of Mr R's relationship with CSS, investment advice was defined in art 53 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001/544 ('the RAO') as:

> *53. Advising on investments*
> *Advising a person is a specified kind of activity if the advice is—*
> *(a) given to the person in his capacity as an investor or potential investor, or in his capacity as agent for an investor or a potential investor; and*
> *(b) advice on the merits of his doing any of the following (whether as principal or agent)—*
> *(i) buying, selling, subscribing for or underwriting a particular investment which is a security or a [relevant investment] , or*
> *(ii) exercising any right conferred by such an investment to buy, sell, subscribe for or underwrite such an investment.*

At the time, the perimeter guidance (PERG) in the FSA Handbook said the following about the meaning of 'advising on investments':

> *Giving a person generic advice about specified investments (for example, invest in Japan rather than Europe) is not a regulated activity nor is giving information as opposed to advice (for example, listings or company news). However, the context in which something is communicated may affect its character; for example, if a person gives information on share price against the background that, when he does so, that will be a good time to sell, then this will constitute advising on investments.*

When asking whether CSS gave investment advice to Mr R, I started by looking at CSS's private client agreement. It says:

2. Definitions

Client Adviser – your client adviser at CSS Partners LLP

4. Services to be provided under this agreement

*We shall provide **advisory** and deal arranging services in the following: -*

Shares in public or private companies;
Debentures in convertible loan stock;
…

5. Investment objectives
*In order to be able to provide you with **investment advice**, it is essential that we understand your investment objectives and your personal financial circumstances. It is important, therefore, that you provide us with as much information as possible in Annex 5 to this Agreement*

9. Material interest/conflict of interest
*We may give you **investment advice** or enter into transactions for you where we or an Associated Company or some other connected person may have an interest…*

*By way of example we might be: i) acting as **financial adviser**, underwriter, placement agent or lending banker to the company whose securities you may be buying…*

Annex 1:
*We may **recommend** transactions to you…**[my emphasis]***

Mr R completed Annex 5 in January 2006 with some information about his financial experience and assets. He also provided information about his investment objectives being to primarily maximise capital growth and that he was prepared to accept a high level of risk in respect of 20% of his investments.

In section 7 on 'Restrictions' it said: *I do not wish to receive advice relating to or trade in any of the following types of investments (for example options, warrants, or unregulated collective investment schemes).* In this section, Mr R stated that he didn't want to receive advice relating to options or warrants (which I think implies he would receive advice on other products).

As we know, Mr R soon after signed a further client agreement for intermediate customers. That agreement was in largely the same terms as the previous private client agreement. Sections 2, 4, 5 and 9, outlined above, were in the same terms and included the same references to 'advice' and 'recommendations'. A different section for intermediate customers was included in annex 2 under the heading Categorisation Notice – Intermediate Customers. I note that in this annex there was a reference in section 1(b) of the annex under 'Customers Understanding of Risk', which said:

*We will not be obligated to warn you of the nature of any risks involved in any of the transactions we **recommend to** or execute for you.*

However, I note that the annex also contained, in section 2, an Investment Objectives clause that said:

2. Investment objectives
*It is your sole responsibility to ensure that transactions effected with or through us are in accordance with your investment objectives and comply in all respects with any legal or regulatory restrictions upon entering into such transactions. **We will not advise you** in relation to such transactions nor will we owe you fiduciary or similar obligations in relation to such transactions**. [my emphasis]***

In turn, and as CSS has said, this in isolation suggests that as a result of Mr R's classification as an intermediate client, CSS wasn't intending to give advice.

I have given careful consideration to all of the terms in the client agreements in order to determine whether Mr R and CSS agreed that an advisory service would be provided. Although CSS says they didn't provide advice to any of their clients (private or intermediate), I think the Private Client Agreement clearly contemplated that investment advice services would be provided. And given that Mr R was asked about his investment objective and attitude to risk, I think he would have reasonably expected to receive investment advice from CSS when he started his relationship with them.

Against this, I do acknowledge the clear wording in the Investment Objectives clause in Annex 2 of the second client agreement that indicated advice would not be given in relation to transactions effected with or through CSS. This was, as I have already decided, included in the agreement as a result of the non-compliant assessment of Mr R as an intermediate customer.

I also note that the nature of Mr R's dealings with his Client Adviser at CSS did not appear to change at all as a result of the signing of the intermediate client agreement in May 2006.

In turn, and looking at the agreement as a whole, I don't think it is reasonable to view the Investment Objectives clause in the second agreement as determinative of whether the parties contemplated that advice would be given. That clause was contained within a client agreement that otherwise contained multiple references to the giving of advice, including a reference to investment recommendations in the intermediate customer section itself (Annex 2, Customers Understanding of Risk).

Having considered the agreement between Mr R and CSS as a whole, it seems that, on balance, the parties contemplated that investment recommendations and advice would be given.

I turn now to a consideration of the nature of the actual dealings between the parties in order to decide whether investment advice was in fact given to Mr R by CSS.

I note that communications with Mr R's Client Adviser at CSS largely took place in telephone calls. Ideally I would have liked to listen to the calls Mr R had with CSS as that would give a clearer indication of what exactly was discussed and how information about the investments was presented, however these aren't available. CSS provided short handwritten diary notes which were recorded by CSS during their calls. Some of these aren't legible. I have carefully read the ones which are and I can see that the bulk of the notes contain information on particular companies which Mr R was recommended to invest in.

I appreciate that recommending a company could be simply a financial promotion, i.e. *an invitation or inducement to engage in investment activity* as defined in the FCA Handbook at the time Mr R invested. I also considered that CSS used the word "advised" regularly in the notes, but in my opinion this was used as a synonym for 'informed of' or 'explained', for example *advised client of product* and *advised of high risk.*

The question is whether CSS did more than this, i.e. that they didn't just objectively present information about investment opportunities; but in fact provided Mr R with a personal recommendation and advised him on the merits to invest in these companies.

I can see that on many of the diary cards, there is evidence that recommendations were made. CSS phoned Mr R and recommended specific companies to him. Some comments indicating opinions or judgements on the merits of the companies were made. In particular I note the following:

18 Apr 2006: *'advised market was growing'*
12 Dec 2006: '*advised that deal was centred around land in Romania, which is to be developed for retail purposes. Advised that value of land expected to increase as planning permission is granted and land price may increase due to Romanian accession to European Union …"*
30 Jan 2007 *'compatibility is promising, hoping to list on AIM after raising'*
18 Apr 2007 *'gave details on OTX Bridge, discussed company's product, target market and potential benefits, strong management team'*
15 Aug 2007: *'advised Romanian deal will not proceed+ advised switching money into Croatian residential property deal. [Mr R] is happy to do this.'*

This is not to say Mr R wasn't told anything about the risks. I appreciate that nearly all notes including the ones above refer to the investments being high risk and that not all notes only include positive information. But giving risk warnings and giving investment advice aren't mutually exclusive. On the contrary, risk warnings should form part of any investment advice given, particularly with high risk investments.

In making my assessment I have also had regard to the handwritten contemporaneous notes taken by Mr R at the time he received the calls from his client adviser. I note that in a number of those notes, there is evidence of comments and opinions given on the merits of investing in the companies in question. For instance, I note the following:

In connection with a phone call on 25 March 2006, Mr R writes:

'very good'
'co [company] could be sold soon"

In connection with a conversation in September 2006, Mr R writes:

'Very confident should be good'
Suggest 30,000 -£27,000
'time scale 18 months-£10k'

In connection with a phone call on 1 November 2006, Mr R writes:

Safe Europe-Looking to list next year,
Log net- to double next year
Wimax mentioned in FT

In connection with a phone call on 1 August 2007, Mr R writes:

'2 years exit – potential for 7.5million after funding'

In a phone call on 20 September 2007 Mr R writes:

'listing in 12 months – 10 -15 x investment'

And in connection with another investment in the same call he writes:

‘list within 1 year 10 x net profit’ and *‘net return 246%’*

In a phone call on 27 November 2007 about a bridge loan, Mr R writes:

’12 months out of this – 8 to 16 times money

In an undated call note Mr R writes:

‘Will sell for 75[p] to £1’
‘Re-list on AIM in 6 months’

I have also considered the following wording, referred to by CSS, which is included on the application forms for investments. CSS says it shows that Mr R was making his decisions based on the written documents that were sent to him and not on their recommendation.

"We confirm that I am/we are applying on my/our behalf, that I/we have read, accepted and understood the terms and conditions set out in the document, that I/we have taken appropriate professional advice before submitting this application form and that I am/we are aware of the risks involved in investing in […]
I/we further confirm that I am/we are applying on the basis only of the information contained in the Placing documents which supersedes all other information (whether written or oral) concerning the company and [the investment]."

However, I think it was reasonable for Mr R to regard his conversations with CSS as having taken *appropriate professional advice* and having been informed of the risks. I’m not saying that he wouldn’t have read the brochures at all before applying for the investment. However, the diary notes show that CSS regularly recommended a company and sent out information material and placement documents to Mr R and then called back a few days later to discuss the investments again presumably after Mr R had received the written documentation. Several notes show Mr R made his decision about how much to invest during these second calls with CSS.

So I think it’s unlikely he would have only relied on the information included in the brochures but would have been influenced by what CSS was telling him in their calls before they sent him the paperwork and after he received it. In summary, I don’t think the wording in the application forms is evidence that Mr R was not relying on advice from CSS when he applied for the shares in question.

I’ve also taken into account correspondence which Mr R sent to CSS indicating he was unhappy with his investments. In my view, there is a consistent reference in the correspondence to ‘advice’ and ‘recommendations’ from CSS. Mr R has consistently expressed his concern regarding overly optimistic judgements and opinions expressed by CSS in connection with the proposed deals they were putting to him.

In August 2010 Mr R sent two letters to CSS saying:

*‘I am very concerned about the current and future safety of the considerable amount of money I have invested in various companies **strongly promoted and recommended** by your company’*

‘Quite simply, I do not feel your company is delivering what I believed I would be getting when I followed ***your 'brokers' advice.***

‘…the various share issues and the repeated additional funding requirements of some of the companies I have invested in makes me think they are ***not as healthy and sound as [member of staff at CSS] has been leading me to think they are****.’*

‘I am fast losing confidence in your company’s abilities to safely invest my money; and in its ability to give ***accurate and honest advice*** *relating to the companies which you supposedly work closely with.’*

A few weeks later he wrote an email saying:

‘*I am now being forced to think I may have been seriously misled* ***by the advice you have given to me*** *regarding the quality and prospects of the companies* ***you have been recommending me to invest in****.*’

In his complaint letter to CSS in July 2011 he said:

‘Can you clarify the position with regard ***to the investment advice*** *I have been receiving from your brokers since January 2006. ‘*

These communications show that Mr R consistently indicated he had received advice from CSS. And I note that in their responses, CSS at no point refuted that advice was given.

All in all, it is my view that on balance CSS gave investment advice to Mr R in the phone calls made to him by his client adviser. I don’t agree with CSS that the client adviser merely gave information about the companies involved. To my mind, there is evidence in the phone notes taken by both CSS and Mr R that suggest comments were made which contained value judgements about the merits of purchasing the shares in question. Speculative information about the likely time frame for listing by the companies, and the potential returns to be made, was in my view given in order to influence Mr R’s decision making about whether to purchase the investments in question and in turn went beyond the mere provision of information.

Further, I’m aware that the phone calls were made to Mr R following a due diligence process of sorts by CSS. CSS completed *Existing client and Suitability Reports* for each investment in which they noted information about how much Mr R was about to invest in a particular company and information about Mr R’s portfolio size with a breakdown of assets. The forms included a tick box labelled “Suitable: Yes” and which had a section where CSS had to sign that suitability was agreed. CSS said this was to establish whether Mr R continued to be suitable as an intermediate client. However, I note that these forms were completed for every investment, even when Mr R was still categorised as a private client. The forms indicate that CSS considered Mr R’s circumstances and financial details before making any recommendation. This in my view gave a context to the calls which suggested the companies had been selected *for Mr R* – again, giving the calls the force of a recommendation.

The recommendations might not have always been explicit, but the context in which they were made, as set out above in PERG, is also important in considering whether advice was given. Having weighed up the evidence, I consider that on balance, Mr R made the investments which are the subject of his complaint as a result of the investment advice he received from CSS.

was the advice suitable?

CSS had to ensure any advice they gave was suitable for Mr R taking into account his financial and personal circumstances including his investment objectives, his attitude to risk and his capacity for loss. They also had to act in his best interest.

Mr R was a self-employed businessman who had sold a family business before and was in the process of selling another one. CSS diary notes in January 2006 record that he wanted to *spend more time in markets* and that he *had lots of previous experience in EIS*. On his client information form to CSS he did note he had several years' experience trading in FTSE 100 and FTSE 250 as well as in AIM and OFEX. Although Mr R now says he didn't have this experience and would never have said so, I have no reason to doubt that the diary note reflects what was said. Mr R says he didn't even know what AIM and OFEX were, but I think on balance he wouldn't have stated he had this experience in these markets without knowing at least what these terms meant.

He told us he had previously received recommendations from a stockbroker and that in the past he had also followed the tips and advice from some of the national newspapers and bought a few shares of the larger well-known companies. He's also since provided investment statements that show he had invested in some high fluctuating shares previously, a small proportion of which seem to have been AIM and pre-IPO. He was interested in investing into small developing companies and his investment objective was capital growth.

Based on the information I've seen I don't think Mr R likely was an expert in pre-IPO shares or other non-readily realisable investments and that he was comfortable to invest large sums without professional advice and support. However, I think he likely had a reasonable understanding of the stock markets and how shares worked. Equally, I think he would have understood that the companies he was investing in were in their early stages and not listed yet. And given his business background I think he also would have understood the many, sometimes unforeseen, difficulties a small business could encounter which would prevent its success and increase their risk.

The diary notes mention throughout that the investments are high risk and warn of illiquidity. And the brochures sent out to Mr R showed that the companies weren't listed yet and reiterated the high-risk nature of these investments prominently early on in the brochures. They said:

…investment in the Ordinary Shares involves a high degree of risk. Any subscriber for the Ordinary Shares must have no need for any liquidity with respect to this investment and must be able to withstand a total loss of his investment. Each potential investor must carefully consider the risks described below and the other information set out in this document before deciding to invest in the Ordinary Shares.

I think Mr R would have had a reasonable understanding of how these investments would work and that they were high risk.

I've also considered the limited investment statements I've seen from the time before Mr R became a client which show funds and shares which were subject to large fluctuations and which indicate he was investing in some higher risk assets. CSS also pointed out that another stockbroker Mr R dealt with around the same time (in 2005/2006) specialised in higher risk investments and Mr R acknowledged that he lost money through them and a compensation claim was upheld. I think this indicates that he was investing into higher risk investments with other companies too.

For clarity, I don't think this means Mr R wanted to take high risk with all of his broader investment portfolio. He also had property investments and liquid savings and I think it's likely some of his previous investments into FTSE 100 and FTSE 250 shares carried lower risk too. So I think in terms of his broader portfolio risk profile, he was likely to be a medium to high risk investor.

But based on what I've seen in terms of the investments he transacted through CSS, Mr R seems to have been happy to invest his money in smaller unlisted companies which he knew would be, broadly speaking, high risk with the potential for high returns.

Given the substantial assets he had I'm also satisfied Mr R had the capacity to take high risk with some of his investments.

The investments he made through CSS, be it shares, bridging investments or loan notes were designed to grow his capital, so met his investment objectives. I consider all of them to be high risk which is supported by the placement documentation for every investment which refers to their high-risk nature. But given Mr R's circumstances and knowledge of how shares and small businesses worked and his attitude and capacity for loss I think the sort of investments recommended to Mr R were generally suitable for him.

The fact they didn't perform as well as he had hoped they would or as CSS might have reckoned themselves, doesn't necessarily mean they weren't suitable. The risk with unlisted and early stage companies is that they might fail. On the flipside they can attract high rewards if they are successful. And I think Mr R knew that. In his complaint letter to CSS Mr R acknowledged *'**Whilst I accept some companies will prosper and some will fail**, your company's record appears to me... to be abysmal. [my emphasis].*

I haven't seen clear evidence that CSS was giving Mr R misleading information with regards to the companies he was investing in. As explained above, the diary notes suggest risk warnings were given and the paperwork reiterated these clearly. Examples of diary notes which mentioned more specific risks are:

22 Mar 2006: Signal- *"explained potential market and risks-trials not completed, science not totally proven"*

8 December 2006: Greencote- *" advised that whilst company looks strong, risk factors included slow processing of orders and difficulty in entering a highly competitive market (no platform in US)"*

12 December 2006- Romanian property deal- *"advised of high risk nature of deal (planning permission not granted, no guarantee of rising land value."*

All investments were described as high risk and illiquid. In his own notes Mr R kept from the calls he noted down CSS said *"Co [company] could be sold soon", "very good", "very confident-should be good", "Lognet-to double next year", re-list on AIM in 6 months", "target investment time-18 months", "listing in 12 months", "150 million annual sales envisaged".*

I don't doubt that CSS told him these were promising investment opportunities and that the information was given in an encouraging tone that was designed to influence his decision making. And I can see that timeframes and possible returns were discussed which largely turned out to be too optimistic in hindsight. But I can't see Mr R was given any assurances or guarantees that these companies would be listed or would be successful. And based on the information available I think Mr R was also reasonably informed of the significant risks. As with most investments a particular outcome isn't guaranteed and it would be unreasonable to expect that any company could foresee specific outcomes. This isn't possible even for listed shares of large established companies and unlisted companies face far higher risks and uncertainties. No adviser could provide guarantees and being a business owner himself, I find it difficult to believe that Mr R might have thought this was the case. I also haven't seen any evidence that CSS was providing Mr R with information that they knew or should have known was incorrect.

It follows that in my view, CSS likely did not give Mr R misleading information about the investments they recommended to him. Further, I consider that Mr R understood how those investments worked and that they were high risk. For the reasons given above I think the investments were broadly suitable for Mr R.

The key question is whether these investments should have continued to be recommended to him to the extent they were and whether at any point further investments became unsuitable when they exceeded Mr R's attitude to risk or capacity for loss or weren't appropriate for his circumstances any longer.

The 25% limit on high risk investments

I think a reasonable starting point is Mr R's client agreement in which, at annex 5, section 6, headed 'Investment Objectives', a term provided:

I am prepared to accept a high level of risk […] in respect of […] of my investments in terms of the acquisition costs of such investments.

Mr R ticked the box after 'high level of risk' and stated he was prepared to take a higher risk on 20% of his investments. He later changed this to 25% when he signed the new agreement for intermediate customers. I appreciate Mr R says he doesn't know why it changed from 20% to 25%, but I think on balance it's likely that he simply decided to take a bit more risk a few months after he started investing through CSS.

In any event, I think CSS could reasonably rely on what Mr R was telling them about his preparedness to take high risk.

The agreement between CSS and Mr R indicated he was prepared to accept a high level of risk in respect of 25% of his investments in terms of the acquisition costs of such investments (I will call this 'the 25% term'). The question is: What, objectively speaking, did Mr R and CSS intend that term to mean?

I note that there has been much said by the parties and their representatives about the meaning of that term.

CSS, in their letter of 29 January 2018 to this service, told us the 25% limit was guidance from Mr R as to

‘*how much exposure he wanted to take at that time and* ***therefore, broadly, how many investments we should offer to him.*** *[CSS’s emphasis]. CSS always kept that broad limit in mind when offering new prospects, but it was always [Mr R’s] sole decision whether to invest in new companies, even in circumstances where we offered him opportunities such that he was close to the 25% figure.*
…
‘the 25% figure was general guidance to CSSP as to which investments CSSP should introduce to [Mr R] and that, based on the information we had at the time, the percentage held in private companies did not exceed the guidance level of 25% of total portfolio.’

They enclosed a spreadsheet in which they calculated the 25% limit in reference to Mr R’s overall investment assets and not just the investments he made through CSS. So in CSS’s view the 25% limit is in reference to Mr R’s overall investment assets.

We spoke to Mr R in April 2016. The call note says:

‘[Mr R] said he did not know all the investments being recommended to him were high risk. He agreed to 20% high risk and thought the other 80% were low risk.
…
He didn't tell [CSS] about changing his ATR as he thought the recommendations they were making were for companies that were not high risk and would do well. He believed they were compiling a portfolio for him.’

In his response to my provisional jurisdiction decision Mr R said:

‘key and fundamental point here is my declared wish to limit any involvement in high-risk shares. Initially I specified that only 20% of my investment could be invested high-risk shares, when they later discussed this with me I think they must’ve persuaded me to increase this profile and I believe I reluctantly made the smallest change I could, to comply with their wishes and increased this to 25%. At no stage did I believe they could legally exceed my request.

So Mr R’s view is that he thought only a quarter of his investments *arranged through or with CSS* should have been high risk.

Whilst I have taken the parties’ views into account, the construction to place on the 25% term in the agreement is, ultimately, an objective exercise, taking into account the agreement as a whole and applying business common sense and reasonableness.

In my view, the sensible, objective construction of the term is that it indicates Mr R was prepared to accept a high level of risk in respect of 25% of the investments he made *with or through CSS*. I do not agree with CSS that the reference to ‘investments’ in the term was a reference to Mr R’s wider investment portfolio or assets. On my reading of the agreement, the word ‘investments’ was used throughout the agreement as a reference to the investments offered by CSS.

I point, for instance, to the following:

> *Clause 6: 'Restrictions' …there are no restrictions on the types of* ***investments*** *or markets …in relation to which we may provide our services to you'.*
>
> *Clause 8: 'Unsolicited real time financial promotions'…we shall telephone or visit you to discuss* ***investments'****…*
>
> *Clause 9: 'Charges and Commissions' …if the* ***investment*** *is being offered without a prospectus, our charges will be specifically disclosed…*
>
> *Annex 4 Clause C: 'Promotional Material' I …do not attach any restrictions on the type of* ***investment*** *upon which I wish to be informed'*

The 25% term itself appears in Annex 5 of the Client Agreement which is headed 'Client Information Form'. Annex 5 consists of seven sections, asking Mr R for information about his personal details, employment, investment experience, assets, liabilities, investment objectives and restrictions. As I say, the 25% term is in section six, headed 'Investment Objectives'. In part (i) of section six, Mr R confirms that his *'investment objectives are a balanced return from income and from capital growth primarily to maximise capital growth'*. To my mind, and in light of the sparse details asked of Mr R in annex 5, those objectives as stated in part (i) can only sensibly be referring to the nature of the investments Mr R wished CSS to offer him.

Immediately following that clause, in part (ii) of section six, the agreement says:

> *'I am prepared to accept a high level of risk in respect of 25% of my investments in terms of the acquisition costs of such investments.'*

From this, I can see there is a common thread in the agreement by which the word 'investment' has come to refer to the investments offered to Mr R by CSS. This is in my view a sensible and natural reading of the agreement. In particular, parts (i) and (ii) of section six should be read consistently to give meaning to Mr R's stated investment objectives. On my reading, Mr R's investment objectives are that he would like CSS to offer him investments that maximise capital growth, but that only 25% of those investments should be high risk.

That construction is, I believe, further confirmed in section 7 of Annex 5, (immediately after the 25% term), under the heading 'Restrictions', where the agreement says:

> *I do not wish to receive advice relating to or to trade in any of the following types of* ***investments*** *(for example options warrants or unregulated investment schemes).*

In this section Mr R writes, *'options warrants, etc.'* Again, the natural meaning of the word 'investments' is the investments offered by CSS.

Against this construction, I have given careful thought to clause 16 of the agreement ('Risk Factors'). This clause does speak directly to the notion that high-risk investments should be confined to a portion, only, of *'your portfolio',* and I acknowledge that in turn speaks to the construction of the 25% term favoured by CSS. Clause 16 says:

> *Investing in private equity and associated investments involves a high degree of risk. Investments should only be considered for that portion of your portfolio which is reserved for more speculative investments. In general each investment which is offered through a Prospectus will outline the risks of that investment in the Prospectus.*

But on my reading, even clause 16 appears to make a clear distinction between the 'investments' offered by CSS and the wider 'portfolio' of the client - and it is clear that 'investments' is a reference to CSS' private equity investments.

Further, I can see that section 5 of annex 4 of the agreement *did* ask Mr R to detail his wider financial circumstances, and that might suggest there was an emphasis in the agreement on the mix between Mr R's wider portfolio and the CSS investments he was offered. But, again, I note that the details in section 4 of annex 5 were referred to under the heading, 'Assets' and <u>not</u> 'Investments'.

In my view, if CSS intended the 25% term to refer to the 'Assets' listed by Mr R in section 4, or the wider notion of his general 'portfolio' in clause 16, I would expect to see those terms used in the 25% term, and not the word 'investments'. Indeed, I would expect to see a good deal more particularity about what 'investments' the 25% threshold was intended to apply to, if the intention was that it should not apply to the investments offered to Mr R by CSS.

I have also given cautious thought to the following wording in the 25% term:

'…in terms of the acquisition costs of such investments.'

It is clear from this that it is the 'acquisition costs' of 'the investments' that are to be used when calculating the 25%. But to my mind, it does not make commercial sense to then say the term *'investments'* refers to the client's wider portfolio or assets. Surely, even on CSS' construction of the meaning of the 25% term, the acquisition costs of the other assets in Mr R's wider portfolio are irrelevant. Why would CSS need to know those costs? What would matter, on CSS' construction, is what those assets were worth at the time they were disclosed to CSS and not what they cost Mr R to purchase in the first place. I don't think the term is workable on the construction CSS gives to it.

But if the word 'investments' is taken as a reference to the investments offered through CSS, then the 25% calculation is workable. In short, Mr R is saying he wants no more than 25% of the investments CSS recommends to him to be high risk. When calculating the 25%, CSS is to take account of the acquisition costs of those investments (and not, presumably, their value taking investment growth into account).

It follows from this that the sensible, objective construction to give to that term is that Mr R was prepared to accept a high level of risk in respect of 25% of the investments he made with or through CSS.

I'm aware that CSS will say that it did not offer any other investments – that it only offered investments in early stage growth companies, which, as I have already found, were all high risk. However, that is not what the agreement with Mr R said. It is plain from clause 4, '*Services to be provided under this agreement'* that advisory and deal arranging services would be offered not only in shares in public or private companies, but also in regulated collective investment schemes such as unit trusts and '*any other investments or instruments as we may agree from time to time*'.

I should also point out also that the 25% term was a standard clause in the agreement. Whilst Mr R ticked a box to say the clause applied to him, and provided the figure of 25%, the term was otherwise part of CSS' standard client agreement. In turn, and to the extent that there was any ambiguity about the meaning of that term, it was incumbent on CSS to take steps to clarify its scope with Mr R. As I understand it, no such steps were taken.

It follows that in my view, at the outset of their advisory relationship, Mr R and CSS agreed that no more than 25% of the investments recommended by CSS to Mr R would be high risk. That means that each time CSS recommended a deal to Mr R, they were required to take his stated risk threshold into account.

application of 25% term

Looking at the investments Mr R made through CSS they were all high risk which means he was always invested 100% in high risk investments. So the originally agreed 25% threshold was breached throughout CSS's dealings with Mr R. Based on their agreement with Mr R, CSS should have included 75% non-high risk investments in their recommendations, which they didn't do.

However, notwithstanding the terms on which Mr R and CSS initially agreed to conduct their business, I have also given very careful thought to the manner in which their business was conducted over time in order to see whether the 25% term continued to apply to their dealings. It's worth noting that Mr R's risk appetite with regards to CSS's recommendations could have changed at any point and in this context I don't think I can ignore Mr R's actions here. I appreciate he told us that throughout his dealings with CSS, only a maximum of 25% of CSS's offers would be high-risk investments and the other recommendations would be low risk. Although I've said that this was contractual basis on which their relationship began, I don't find it plausible to say that this is how Mr R continued to indicate his attitude to risk to CSS as the relationship unfolded. As explained above, based on the evidence I've seen, I think Mr R likely knew that the investments recommended to him by CSS were all high risk, and further, that he understood the implications of that. And I can't see that he ever raised this with CSS as an issue at any point during their advisory relationship.

What I think is more likely is that, despite the risk, Mr R wanted to continue to access the investment deals recommended by CSS and was prepared to make more high-risk investments through CSS over time than he originally might have intended.

I appreciate CSS didn't follow the original agreement or alternatively didn't check with Mr R at any point if he was willing to invest more than 25% into high risk investments which I think they should have done. But given that Mr R to my mind knowingly accepted recommendations into high risk investments through CSS, I think shows that he was prepared to invest more into high risk investments than he originally agreed. On balance I think Mr R made an informed choice to invest purely in high risk investments through CSS and he was prepared to take that risk.

Even if CSS had broached the 25% term with him, as I have said they should have, it is my view that he would still have wanted to invest in the high-risk investments he eventually transacted with CSS. That appears to be the reason he approached CSS in the first place. He wanted to access investment possibilities in early stage growth companies. CSS offered a relatively niche service in that regard. I'm satisfied that, notwithstanding the investment objectives he initially agreed with CSS in the 25% term, it became clear over time that Mr R was happy for CSS to only propose the venture capital opportunities it specialised in.

Having said that, CSS still had an obligation to make sure the investments were suitable. As I have previously decided, CSS wrongly classified Mr R as an intermediate customer. In turn, CSS was required to treat Mr R as a private client and was therefore required to ensure the investment advice it gave him was suitable, taking into account the information Mr R had disclosed or any other relevant facts of which CSS should have been aware.

did CSS's recommendations continue to be suitable for Mr R?

As I have outlined above, I consider each investment made through CSS was suitable for Mr R given his attitude to risk and likely understanding of the risk he was taking. Nonetheless, the suitability assessment also required CSS to make sure Mr R had the required capacity for loss - in other words CSS had to have regard to the level of investment loss he was financially able to bear. CSS had to make sure that they stopped recommending high risk investments when they reasonably considered his capacity for loss had been reached, even if Mr R might have been prepared to carry on investing. Where attitude to risk is a subjective and emotive response to risk which Mr R could change, capacity for loss is an objective measure which CSS had to assess for Mr R. They had to act in his best interest.

In applying this standard, I have taken account of relevant law and regulations; regulators' rules, guidance and standards (including COB 5.3 and COBS 9.2); and what I consider to have been good industry practice at the relevant time.

Ultimately, I consider it fair and reasonable to expect CSS to have stopped recommending high risk investments to Mr R at the point at which he was no longer financially able to bear the loss should those investments fail.

And I think CSS acknowledged that this was something they should have considered. In an email to us in November 2016 CSS said:

Mr R did inform the firm in 2006 that he had sold his business for some £750,000, which reassured us that the ***quantum of money*** *he was investing in the opportunities we were presenting* ***was appropriate to his circumstances.*** *[my emphasis].*

In their existing clients and suitability reports they recorded information about Mr R's overall investments, so based on what they've said I think it's reasonable to assume they were recording this to monitor the amount Mr R was investing compared to his available funds and in turn to ensure their recommendations were still appropriate with regards to his capacity for loss.

I can see that CSS didn't have enough information to fully assess Mr R's capacity for loss with what I would call reasonable precision. They didn't know his income and outgoings, how exactly his other assets were invested and in what way he relied on the funds invested with CSS. And I don't know how much information Mr R would have given CSS if they had asked him. They were only advising him on certain investments and weren't his financial advisers with regards to his overall financial situation. So it's possible Mr R might not have wanted to divulge full information about his overall financial position. I think the limited information he did provide on the client forms supports this. And a call note after a conversation between Mr R and this service in April 2016 recorded:

'He said he was modest with the amount he declared, and was quite modest in his assets. He scaled down things rather than being flamboyant. He got money from the sale of his business and also inherited from his parents. He used some of that money to make the investments'.

Given the above it's unclear to what extent Mr R would have provided information to CSS if they had asked further questions. I also think it's difficult now to establish with enough certainty Mr R's full financial situation at the time the investments were made. So I have considered what conclusions CSS should reasonably have reached about Mr R's capacity for loss, given the information they had available.

Although as explained above the 25% term in the client agreement related to Mr R's preparedness at that point to invest into high risk investments with CSS (which I think changed over time), I nonetheless think 25% was a reasonable measure for CSS regarding Mr R's *capacity for loss* in the circumstances.

CSS themselves said they kept Mr R's limit on the client form *broadly in mind* when making their recommendations and that *the 25% figure was guidance* to them about which investments they *should introduce* and that the percentage in high risk investments compared to his total portfolio didn't exceed this limit.

I also considered that Mr R's former representatives said in an email to this service after a previous decision by this service in February 2018:

'we are in agreement with the ombudsman that [Mr R]'s net investment value at the time was around £900,000, 20-25% of this is between £180,000 - £250,000. This should have been used as a defined figure for [Mr R's] ***capacity for loss*** *by CSSP.'* [my emphasis]

And Mr R hasn't refuted at any point during this complaint that using this methodology was unreasonable and that he had in fact a lower capacity for loss. So I think on balance together with the limited information we do hold about Mr R's financial situation over his investment period with CSS, it is reasonable to assume Mr R could afford to lose 25% of the portfolio value he had declared to CSS.

I don't think CSS could reasonably assume without more information that his capacity for loss was higher than this. I think they also should have borne in mind that the investments Mr R was entering into were not just high risk to the point where they could fluctuate, lose value or take some time to come to fruition. There was a genuine risk that Mr R could lose all of the capital he was investing. Holding 25% of a total investment portfolio in such assets is already high in my opinion and I would say many investors would not have the capacity to even lose this much.

Looking at the portfolio information Mr R did provide to CSS and for reasons set out above I think he likely did have this level of capacity for loss. But I'm not convinced it would have been any higher than 25%. So on balance I don't think it was appropriate for CSS to recommend any investments to Mr R which meant his CSS investments exceeded this limit.

what would Mr R have done if CSS had stopped recommending investments?

As I explained before I think Mr R was prepared to invest in high risk shares and I have found that, even if CSS had taken steps to clarify the 25% term with him, he would more likely than not have continued to invest into the higher risk investments CSS were proposing to him.

However, I don't think that would have been the case if CSS had told him at the required point that, based on the information they held, he had reached his *capacity for loss* limit. CSS should have explained to Mr R that in their view the amount he had invested in high risk investments had reached a loss limit they thought he couldn't reasonably afford to exceed given his financial circumstances and that in turn they would not be recommending any more high-risk investments to him as it wasn't appropriate. If they had explained this, I don't think Mr R would have insisted on continuing to invest in this way. From what I've seen it looks like CSS was generally initiating contact. So if they had told him they would stop recommendations and did not call him anymore for a while, I think it's more likely than not he wouldn't have actively pursued high risk investments through them. It follows that he wouldn't have ended up with investments through CSS which breached that limit.

I have considered whether Mr R might have continued to invest in similar high-risk investments elsewhere even if CSS had stopped recommending such investments to him. CSS provided evidence that Mr R bought shares of private companies in 2012 and 2015 without CSS's involvement (Eastern Continental Mining and Development Ltd and Arro Supranano Ltd) which they say shows he still had an appetite for high risk investments even after his dealings with CSS.

I accept that there is evidence that Mr R did invest to a small extent in private companies a few years after his relationship with CSS had ended and I think it's reasonable to assume that Mr R continued to be interested in this type of investment. However, if CSS had made it clear they were concerned about Mr R's ability to absorb more losses from high risk investments and had told him he shouldn't invest more into high risk investments as higher losses would have a detrimental effect on his overall financial situation, I think he would have listened to CSS' concerns and invested his available funds in lower risk investments for a while. In any event, I don't think he would have invested to the same extent into high risk investments as he did with CSS.

Nonetheless, I also considered what likely would have happened if Mr R had approached a different firm for the same kind of high-risk of investments directly after CSS stopped their recommendations. And I think on balance after reviewing Mr R's financial situation and taking into account his existing investments with CSS, it's likely they also would have found it was inappropriate for Mr R to invest further into high risk investments. If it was an adviser firm they would have likely recommended against further high-risk investments and even financial businesses who only promoted high risk investments would likely have found it was inappropriate to promote high risk investments to Mr R given his existing exposure compared to his financial situation.

In summary, I think Mr R on balance wouldn't have looked elsewhere to invest the same way he did with CSS after they had stopped their recommendations and warned against further exposure to high risk investments. And even if he did, I think he would have found it difficult to find another firm that was reasonably prepared to deal with him in respect of similar types of high-risk investments at this point.

fair compensation

In assessing what would be fair compensation, I consider that my aim should be to put Mr R as close to the position he would probably now be in if he had not been given unsuitable advice.

I think any funds he wouldn't have invested through CSS (at the point they breached his capacity for loss) would still have been invested but would have been invested differently by Mr R. I don't know exactly what he would have invested in instead. However, and in line with my assessment of his broader portfolio risk profile above, I am satisfied that what I have set out below is fair and reasonable taking that into account and given Mr R's circumstances and objectives when he invested.

how should the 25% capacity for loss limit be assessed?

I think it's reasonable in the circumstances to consider that CSS should have based their assessment whether Mr R had the capacity for loss on the financial information they had recorded about Mr R's investment portfolio. I appreciate CSS says Mr R's investment portfolio might have had a much higher value, for example they referred to a commercial property he held in his self-invested personal pension that they weren't aware of at the time. And given what Mr R said to this service about being modest in his declarations to CSS, this is quite likely. The argument here would be that a higher portfolio value would mean a higher capacity for loss in monetary terms.

But I think CSS could only consider suitability based on the information available to them. If Mr R had overstated his assets I equally would expect CSS to be able to rely on this information and not on Mr R's actual assets at the time.

The value of Mr R's investments that was known to CSS changed over time. In January 2006 Mr R said he had £100k in tradeable investments and £50k in liquid savings. Over time the value increased. Whenever an investment was made CSS recorded Mr R's portfolio size and the information they held was regularly verified with Mr R. I've seen financial information reports which were sent to him and which he amended where he saw necessary, so I think it's reasonable to rely on these values.

On 9 July 2009, when making his last investment through CSS, his portfolio size was recorded as £1.735,710.85 which was broken down as:

Tradeable investments: £135,750
Liquid savings: £70,000
Peps ISAs: £150,000
Private/unquoted companies: £639,960
2nd property: £740,000

These values included all of the CSS investments including the one he was about to make. I know that CSS said Mr R sold his company for £750,000 and when they previously calculated Mr R's percentage of CSS investments they added this sum to Mr R's portfolio from September 2007, but I can't see what information they were actually given about this by Mr R and at what point.

The diary notes in January 2006 show that Mr R was in the process of selling his business and it looks like that this sum was mentioned, but in March 2006 the notes record he sold his business for over £100k and a couple of weeks later it's noted the sale fell through. Mr R has also mentioned the sale of his company, but I haven't seen any other evidence to show what information Mr R had given CSS about the sale of his business after that.

The proceeds of the sale also weren't specifically considered in the portfolio size when CSS completed their records before every investment. There is no mention of it. Unless CSS can provide further evidence, I can't see that CSS knew for how much and when Mr R sold his business and what had happened to these funds. Any increases in the recorded portfolio value which weren't down to CSS investments could have in theory also been funded from the sale of his business, for example the increase in savings, tradeable assets or the higher value of a second property which was recorded by CSS. So I don't think CSS could have considered this sum in addition to the portfolio values when assessing Mr R's exposure to high risk investments, without clearer information from Mr R about the business sale.

I think it would have been clear to Mr R that CSS weren't providing advice on his overall financial situation and could only consider information they had. He was advised by CSS to provide as much information about his financial situation as possible and I think in these circumstances it's reasonable for CSS to only consider the information they were provided by Mr R and apply his capacity for loss limits to these values.

Before recommending an investment, I think CSS should have referred to the current portfolio size on their existing client and suitability report (amount set out under *'Total'*) and worked out whether this next investment would take Mr R's CSS portfolio above his 25% capacity for loss.

Using these numbers on the CSS reports and the investments Mr R made (see table below), I consider that the last suitable investment recommended to Mr R was the *Miras* investment on 7 August 2006 for £11,250. <u>Every investment after this date exceeded Mr R's 25% capacity for loss limit, so was an unsuitable investment that shouldn't have been recommended</u>. It follows Mr R wouldn't have invested £430,152.66 with CSS.

what should CSS do?

To compensate Mr R fairly, CSS must:

2) compare the performance of Mr R's unsuitable investments with that of the benchmark shown below and pay the difference between the fair value and the actual value of the investments. If the combined actual value is greater than the combined fair value, no compensation is payable. CSS should also pay interest as set out below. Income tax may be payable on any interest awarded.

investment name	benchmark	from ("start date")	to ("end date")	additional interest
Unsuitable investments in CSS portfolio (as	FTSE UK Private Investors Income Total	date when each unsuitable investment	date of my final decision	8% simple per year from date of decision to date of settlement (if compensation is not paid

identified above)	Return Index	was made		within 28 days of the business being notified of acceptance)

Actual value

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

If at the end date an investment 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 R agrees to CSS taking ownership of the investment, if it wishes to. If it is not possible for CSS to take ownership, then it may request an undertaking from Mr R that he repays to CSS any amount he may receive from the investment 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.

Any withdrawal, income or other payment out of the investment 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 are a large number of regular payments, to keep calculations simpler, I will accept if CSS totals all those payments and deducts that figure at the end instead of deducting periodically.

why is this remedy suitable?

I have chosen this method of compensation because:

- Mr R wanted capital growth from the investments he purchased through CSS and was willing to accept high investment risk in connection with those investments.
- However, CSS should not have recommended investments that exceeded Mr R's threshold for capacity for loss of 25% of his wider financial portfolio that was known to CSS.
- If CSS had explained that threshold for loss to Mr R and stopped recommending high risk investments, Mr R would likely not have invested the level of money he did in high risk investments through CSS or elsewhere.
- He would still have invested the money that exceeded his 25% threshold for loss and any alternative investments would likely still have a reasonable amount of 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

R's circumstances and risk attitude.

I appreciate CSS think this benchmark doesn't reflect sufficiently that Mr R was likely to continue in high risk investments be it through CSS or elsewhere. However, and as I've outlined above, I'm satisfied that on balance and following the explanation of his capacity for loss, Mr R would not have invested all sums he didn't invest through CSS into the same category of high-risk investments elsewhere. So I think on balance the index used is reasonable in these circumstances.

my provisional decision

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £150,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £150,000, I may recommend that CSS pays the balance.

Determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My provisional decision is that CSS should pay the amount produced by that calculation up to the maximum of £150,000 plus any interest set out above.

Recommendation: If the amount produced by the calculation of fair compensation exceeds £150,000, I recommend that CSS pays Mr R the balance plus any interest on the balance as set out above.

If CSS does not pay the full fair compensation (including the recommendation if fair compensation exceeds £150,000), then any investment currently illiquid should be retained by Mr R. This is until any future benefit that he may receive from the investment together with the compensation paid by CSS (excluding any interest) equates to the full fair compensation as set out above.

CSS may request an undertaking from Mr R that either he repays to CSS any amount Mr R may receive from the investment thereafter or if possible, transfers the investment at that point.

my provisional decision

I intend to uphold Mr R's complaint and request Charles Street Securities Europe LLP to pay the compensation as set out above.

Nina Walter
ombudsman