complaint

Mr M complains, through his Independent Financial Adviser (the IFA) that Octopus Investments Limited:

- Didn't action his request for full withdrawal from the Enterprise Investment Scheme (EIS) he had invested in.
- Didn't carry out proper due diligence with regards to the investment.
- Didn't communicate with him about what was happening with his investment between November 2015 and September 2018.

background

Mr M invested in the Octopus EIS 3 in 2007. It wrote to the IFA on 8 July 2011 to inform him that some of the companies in the scheme had completed the three-year minimum qualifying period with the remainder to complete by early November 2011. It set out the three options Mr M had, which were to; retain the investment; request a transfer into a new tranche of Octopus EIS; request an exit from the fund.

Mr M intended to switch to a new EIS, but this didn't come about so he decided to remain invested. He was notified that there would be annual withdrawals opportunities from the scheme. Octopus consolidated the investment so that it was concentrated in just one unquoted company, Ticketus 5 (Ticketus) instead of several unquoted companies.

Mr M decided to take advantage of the annual liquidity event he was notified of in October 2012 and withdraw from the scheme. He was told this would be done by February 2013. But in January 2013 Octopus wrote to him to inform him that it could not surrender the whole investment as part of the Ticketus investment involved purchasing tickets from Rangers Football Club (RFC) which had gone into administration, and then into liquidation in late 2012. He received a partial payment of £67,805 from his investment with £14,275 being retained in relation to the part of the investment by Ticketus in RFC.

I issued a provisional decision on the complaint a copy of which is attached and forms part of this final decision. I didn't uphold the complaint. In summary I made the following findings:

- The responsibility for ensuring that the investment was suitable for Mr M was the IFA's, not Octopus's.
- The use of the word 'protected' in reference to the EIS didn't mean there was capital protection and Mr M accepted he was aware the scheme was higher risk.
- I wasn't satisfied that the use of the word 'protected' was misleading or did mislead Mr M as to the risks of the scheme.
- By consolidating investment in just one company Octopus was in breach of the Brochure and terms and conditions, which referred to investing in at least four companies.
- Consolidation may have led to a reduction in administration costs but there was nothing in the documents which indicated Octopus could invest in less than four companies.
- But consolidation didn't increase the risk of the investment because the companies invested in the same assets.
- I wasn't satisfied that Mr M would've chosen not to invest if he had been aware of the consolidation and the reason for this.

- Ticketus didn't loan money to the prospective new owner of RFC as the IFA has stated more than once, the money it paid was for purchase of future tickets.
- Octopus's due diligence wasn't limited to a personal guarantee from the prospective new owner. It included; guarantees from two companies involved in the purchase; a questionnaire; reviewing business plans with future senior management; reviewing full accounts, asset values and squad value.
- The potential tax liability was a risk, but I don't think this made the investment inappropriate.
- Octopus was not able to action Mr M's request for full withdrawal given RFC had gone into administration in early 2012 and was placed in liquidation in October 2012.
- The IFA was wrongly told in January 2013 that the investment was due to pay out full withdrawals in February 2013 but there is nothing to show this caused Mr M any loss.
- I wasn't persuaded that Octopus hadn't kept Mr M informed of what was happening.

I gave both parties the opportunity of providing further information before making my final decision. The IFA didn't agree with my provisional decision. In summary it said the following on behalf of Mr M.

- It wasn't RFC that approached Ticketus, but the prospective new owner of the club through his limited company Wavetower.
- The point it was making is how could Ticketus loan money to someone for future ticket sales on a club that person didn't own at the time?
- Ticketus paid £24 million to the prospective new owner's solicitors a month before the purchase was completed.
- How could Ticketus release £24.4 million to the lawyers before the sale of the club had been agreed?
- It appreciates that Octopus didn't just rely on a personal guarantee, but the questionnaire appears to be a self-certification document, and Octopus hasn't explained what other measures it took to validate his credentials.
- It could've carried out a basic Companies House search which would've shown the prospective new owner had no record of being a company director in the previous seven years, let along experience of running a football club.
- When the new owner didn't make the first payment to Ticketus, Octopus went on to lend further money on future ticket sales.
- In court a judge said that Ticketus had no claim against the assets of RFC, so it was ruled it was investing in the new owner not the club.
- It would like to understand what the ombudsman feels is an appropriate level of due diligence and what evidence has Octopus provided to allow the conclusion it carried out sufficient due diligence?
- Octopus wasn't qualified to decide whether it was likely the potential tax liability to HMRC was payable.
- It is reasonable to assume Octopus would've understood the severity of the situation with HMRC and the risk that RFC could go into liquidation.
- If full withdrawal wasn't possible why did Octopus state in its email of 14 January 2013 that full payment would be made at the end of February 2013.
- Octopus has a duty to provide clear information and using the word 'protected' was misleading and we are surprised that the ombudsman and the FCA aren't concerned with the use of the word in reference to this high-risk product.
- It doesn't agree with Octopus's reasons for changing to investment in only one company instead of the minimum of four required.

- It doesn't agree that this didn't change the risk and the investment in Ticketus companies should be considered as the same investment anyway.
- Investing just in Ticketus meant that the investment changed from a portfolio EIS to a single company EIS, which absolutely would've changed the risk profile.
- It believes that Octopus was aware of the difficulties Ticketus was facing when the original exit was facilitated for investors.

my findings

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

I have considered all the points made by the IFA in response to my provisional decision and note the questions he has raised about the ticket purchase agreement. But I am not required to address every point in my findings, and it is not my role to provide answers to all the questions he has put.

My role is to consider the complaint that Mr M has made and decide if Octopus has done anything wrong, with my findings being made on a balance of probabilities – what is more likely than not – based on the available evidence. The IFA has provided no new evidence that would lead me to change the findings in my provisional decision.

Regardless of when Ticketus paid the money for future season tickets and to whom I'm satisfied on the information I have seen that it is more likely than not it had an agreement with RFC for future season tickets.

The IFA has referred to a judge saying Ticketus had no claim on the assets of RFC and that this means it was ruled that its agreement was with the new owner. The judge – in an application by the administrators for RFC – did say that Ticketus only had a personal right (rather than a security right, trust interest or property right) to performance of the contract by RFC. This shows that the judge accepted there was an agreement between Ticketus and RFS, not that he thought the agreement was with the new owner.

I note the IFA has said it wants to understand what I think is an appropriate level of due diligence. But what I need to do is consider whether the due diligence carried out by Octopus was reasonable or not, rather than specify some notional 'level' of due diligence. I don't think the due diligence carried out by Octopus, as set out in my provisional decision, was unreasonable in the circumstances.

The IFA has again said that the word 'protected' in the brochure was misleading and he is surprised I am not concerned about the use of the word in relation to this this 'high-risk' product. But It isn't enough to simply refer to the word 'protected' and say it is misleading when the brochure didn't provide any information about any such protection.

The suggestion that this was misleading is also inconsistent with Mr M's own evidence that he understood the investment was higher risk and he might not get back the same value as he put in. The IFA also made no mention of the investment having protection in the suitability letter he sent to Mr M.

The IFA has again argued that changing from several unquoted companies to one company increased the risk of the investment. But given these were unquoted companies that all invested in the same assets I'm not satisfied that this did increase the overall risk of the

portfolio in any significant way. I note the IFA has referred to this increasing the concentration risk, but this would only really be the case if the companies had invested in different assets, but they didn't.

Even if using one company did increase the risk, I'm not persuaded that Mr M wouldn't have gone ahead with the investment if he had known this beforehand, given he didn't take issue with this when he was made aware of the change. At the latest I think this was January 2012 when portfolio valuations were sent to both Mr M and the IFA which clearly showed that Mr M's portfolio was only invested in Ticketus 5. And Mr M and the IFA continued to get six monthly valuations and didn't raise any issue about this.

I note the IFA's belief that Octopus knew of the issues Ticketus faced, when it facilitated the original exit from the investment. But I have seen no persuasive evidence that Octopus was aware of information which meant it was aware there were issues with the investment that might affect later withdrawals.

In summary I am not satisfied on the evidence provided that Octopus did anything wrong in its management of Mr M's portfolio.

my final decision

I don't uphold this complaint for the reasons I have explained above and in my provisional decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 27 September 2020.

Philip Gibbons
ombudsman

COPY PROVISIONAL DECISION

complaint

Mr M complains, through his Independent Financial Adviser (the IFA) that Octopus Investments Limited:

- Didn't action his request for full withdrawal from the Enterprise Investment Scheme (EIS) he had invested in.
- Didn't carry out proper due diligence with regards to the investment.
- Didn't communicate with him about what was happening with his investment between November 2015 and September 2018.

background

Mr M invested in the Octopus EIS 3 in 2007. It wrote to the IFA on 8 July 2011 to inform him that some of the companies in the scheme had completed the three-year minimum qualifying period, with the remainder to complete by early November 2011. It set out the three options Mr M had, which were to; retain the investment in the current EIS; request a transfer into a new tranche of Octopus EIS; request an exit from the fund.

Mr M intended to switch to a new EIS but this didn't come about so he decided to remain invested in EIS 3. He was notified that there would be annual withdrawals opportunities from the scheme. The scheme was consolidated by Octopus from investment through several companies to investment through just one Octopus company, Ticketus 5 (Ticketus).

Mr M then decided to take advantage of the annual liquidity event he was notified of in October 2012 and withdraw from the scheme. He was told this would be done by February 2013. But in January 2013 Octopus wrote to him to inform him that it could not surrender the whole investment as part of the Ticketus investment involved purchasing tickets from Rangers Football Club (RFC) which had gone into administration and then into liquidation in late 2012. He received a partial payment of £67,805 from his investment in EIS 3 with £14,275 being retained in relation to the part of the investment in RFC.

Octopus didn't uphold the complaint. It said that all EIS investments are high risk, and that this is what it would've expected the IFA to have told Mr M when advising him about investing in the EIS. It said the brochure it provided for investors prominently outlined the risks. It said that as the discretionary investment manager it was able to offer a range of products that targeted different objectives and its role was to convey accurate information about these which it did for the EIS Mr M invested in. It said it was reasonable to conclude that Mr M was prepared to accept a higher risk to capital when he invested in 2007.

Octopus explained it didn't invest in RFC but into Ticketus companies held in the portfolio and that it chose to use the companies' capital through LLP structures, which approach had been agreed with HMRC. It said that there were therefore groups of companies trading in ticketing-based activities who could contribute capital to a partnership that conducted the deals. Octopus said that following investment the Ticketus companies entered into multiple successful arrangements with event providers. It said the investment in 2011 with regard to RFC followed two previous transactions involving RFC which had provided expected returns.

One of our investigators considered the complaint but didn't think it should be upheld. She said that Octopus confirmed in January 2013 that a full withdrawal wouldn't be possible. She said it did what it could to allow Mr M to withdraw as much as possible from his investment but that there was a shortfall which is tied up in legal proceedings. She said that even if Octopus had told investors earlier in 2012 about issues with regard to RFC there wasn't an opportunity for investors to withdraw their money sooner.

The investigator also didn't think Octopus had failed to carry out appropriate due diligence and said she was satisfied it hadn't just relied on personal guarantees from the club owner and the risks of the investment were clearly set out in the fund brochure. She said that the decision to consolidate the investment in one company was a restructuring decision which we wouldn't comment on.

The investigator also said that Octopus had kept Mr M updated with what was happening with six–monthly statements and meetings with his adviser in 2016 and 2017 and she didn't think any more was required given the situation hadn't really changed.

The IFA didn't agree with the investigator. In short, he made the following points:

- Octopus marketed the EIS as investing in a portfolio of companies which would suggest that it was not a concentrated risk. But when it came to re-investing it didn't make Mr M aware it was going to consolidate the investments into one company – Ticketus 5 – substantially increasing the level of risk he was exposed to.
- Due diligence was not carried out on the new owner of RFC as he can't see where his credible history came from, given he was disqualified from being a Director for seven years in 2000.
- Octopus loaned the new owner £24.4 million personally against RFC future season ticket sales when at the time of the loan the sale of RFC had not been completed. This personal loan elevated the risk that Mr M was exposed to.
- The new owner only set up the company Wavetower in September 2010 and it was connected to Prichard Stockbrokers and Liberty Capital amongst many others.
- If the new owner was able to offer a personal guarantee why was he unable to satisfy RFC he could complete the purchase without the loan.
- RFC entered a dispute with HMRC in 2009 about a possible £49 million tax bill.
- Regardless of previous good ticket sales, as RFC was already in serious financial trouble, loaning so much as against future ticket sales over such a long period was foolhardy.
- Why was it requested that the deal be kept quiet?
- Regardless of whether it would've made a difference, ongoing updates and information should've been provided to Mr M.
- It is denied that he had two face to face meetings with Octopus.
- Mr M was given mixed messages as to his investment risk and no clear explanation of the structure he was invested in.
- Mr M was told to expect the full amount due to him but the time for payment has come and gone several times and he has still not received this.
- In essence he is asking that we don't look at Mr M's complaint as an EIS complaint as such but as a complaint against the activities of Octopus and Ticketus in regard to the relationship between them and the new owner and how he passed their due diligence to personally borrow the amount he did.

The investigator asked for Octopus's comments on the points raised by the IFA and, in summary it made the following points:

- The IFA is incorrect and misleading in what he has said about the level of risk increasing because investments were consolidated into Ticketus 5. The EIS always carried a concentration risk as diversification isn't a characteristic of the investment. The companies were all co-parties on the same deals and contributed to the overarching partnership conducting the deals and were consolidated after three years which reduced administrative costs and wasn't possible within three years as this would've made them non-EIS qualifying.
- They carried out due diligence through a Directors questionnaire that the new owner of RFC responded to and to which he answered no to the question about being disqualified as a Director and answered other questions falsely as well. Ticketus only became aware he had been previously disqualified in an article in 'Private Eye' which referred to him hiding this also from football and City regulators. This was after RFC went into liquidation.

- Ticketus didn't loan the new owner £24.4 million personally, it bought future tickets in RFC and obtained guarantees.
- Guarantees were obtained from Liberty Capital, Wavetower (now Rangers FC Group Limited) and the new owner personally. It also obtained a net worth statement from the new owner showing net assets above the amount of the Ticketus investment.
- It isn't unusual for a person to use third party finance even if they have sufficient funds to finance a transaction.
- It couldn't be foreseen that the new owner was in breach of his directorial obligations and deliberately misled multiple parties including Ticketus, other creditors, the Scottish FA and City regulators.
- At the time of the Ticketus transaction the risk of a substantial tax bill was a potential concern but wasn't considered likely, and the various guarantees provided additional comfort.
- It has provided regular summary updates to investors and no communication would be made about legal recoveries until these were concluded. It has had several meetings with consumer representatives and would expect them to relay what was said to their clients.
- There were meetings with the IFA as it has previously stated and it is surprised this has been denied by the IFA.
- It was the IFA's responsibility to ensure Mr M was aware of the risks of the EIS and what he was investing in.
- The misrepresentations of the new owner have nothing to do with the risk profiles of this EIS or any EIS, or with the structure of discretionary managed investment service.
- The complaint should be considered as a complaint about the EIS and not anything else.

As agreement hasn't been reached the matter has been referred to me for review.

my provisional findings

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

I have set out the main points made by the IFA in response to the investigator's opinion, but I am not going to comment on every point as I don't think they are all relevant to the issues in this complaint.

Octopus was not responsible for making sure that its Protected EIS was suitable for Mr M - that was the responsibility of the IFA who advised him about investing in the scheme. So, it was for the IFA to be satisfied that the EIS was in accordance with Mr M's objectives and his risk appetite.

Mr M has said that marketing the scheme as the Octopus *Protected* EIS was misleading. My understanding of the use of the word 'Protected' in the context of the EIS is that this refers to the scheme investing in companies that targeted capital protection rather than capital growth. That does not mean that Mr M's capital was protected in some way, as I think both he and the IFA will have known.

He has confirmed that he understood from the outset that an EIS is a higher risk investment type, so I think he was aware his capital was at risk and there was no protection, and there was nothing in the brochure that suggested such protection existed.

I note that the brochure does refer to the scheme as 'lower risk' but I think it is reasonably clear that this is by reference to typical EIS schemes and doesn't indicate that the scheme was low risk in comparison to other types of investment – and, as I have said, Mr M has acknowledged he was aware the scheme was a higher risk type of investment in any event.

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Also, the Introductory page of the brochure identified two advantages of its scheme, the first headed 'Tax benefits' and the second headed 'Lower Risk' and under this second heading it states:

"The Fund will be investing in UK smaller companies, a core area of expertise at Octopus. The companies will be known to the team at Octopus and will operate in sectors where there is a high

degree of predictability. These companies are expected to have contractual revenues from financially sound customers and will provide investors with an ability to cash in their investment as soon as possible after three years (the minimum holding period required to retain the initial income tax relief).”

I think this made it reasonably clear the basis on which Octopus was using the words ‘lower risk’ and that it was not stating the EIS was a low risk investment.

The Brochure also explained the risks of the investment and included the following:

“Investments made by the Octopus Protected EIS, because they are in unquoted companies are likely to be higher risk than securities listed on the London Stock Exchange Official List.

Investments in shares in unquoted companies are not readily marketable and the timing of any realisation cannot be predicted.”

In the circumstances, for the reasons I have set out, I’m not persuaded that the brochure was misleading because it used the word ‘Protected’ in reference to the EIS or that Mr M was misled by the use of that word.

The IFA has suggested that because the brochure stated that investment would be into a portfolio of companies that this indicated it was not a concentrated risk and that on reinvestment by Mr M it didn’t make him aware the investment would be concentrated just in one company.

Octopus was the discretionary manager of EIS 3 so could make decisions as to what the scheme invested in as long as this was in accordance with the objective/s of the scheme. The objective of the scheme was clearly tax relief, as the Brochure made very clear. By investing in companies that were EIS qualifying Octopus invested in accordance with the objective.

But the Brochure states, under the heading ‘Investment Strategy’, that:

“The fund will invest in at least four EIS qualifying companies with a view to minimising risk to capital. The investments will be into companies known to the team at Octopus.”

I also note that the terms and conditions of the scheme included the following:

“6.3 We will acquire for your Fund investments which we reasonably believe to be Qualifying investments at the time of acquisition……...Subject thereto, there shall be no restriction on the amount invested in any one investment or on the proportion of your Fund in any one investment or any particular type of investment or on the markets on which transactions are effected unless specified in the Brochure , save only that no more than 50% of the Fund will be invested in any one company and the Fund will invest in at least four companies.”

So, by investing wholly in one company Octopus appears to be in breach of both the Brochure and the terms and conditions of the scheme. I acknowledge the explanation Octopus has given about the companies investing in the same assets - so that consolidating in one company didn’t increase the risks of the EIS scheme. I also accept that there may have been financial benefits, by way of reduced administration costs. But there is nothing in the Brochure or the terms and conditions which indicated that it would, or could, invest in less than four companies.

Having said that I must consider what the consequences of it doing this were. I accept that this didn’t change the risk of the EIS scheme in any meaningful way given the companies invested in the same assets. I also don’t think that Mr M would’ve chosen to withdraw his money from the scheme in 2011 instead of deciding to continue with it if he had been told the investment would be consolidated in one company. There is nothing to suggest he was unhappy with the scheme in 2011 when he was deciding what he wanted to do. So, I think it is more likely than not that if he had been told of the consolidation and the reasons for this, he would still have decided to leave his money in the scheme.

I turn to what I consider the main issue in this complaint which I think is whether or not Octopus carried out sufficient due diligence in relation to Ticketus purchasing future tickets in RFC. I think it is reasonable to expect a discretionary fund manager to carry out appropriate due diligence on the investments they are making under the mandate that has been given and a failure to carry out reasonable due diligence will be a breach of their obligations to the client under the mandate.

I think it is important to be clear about what Ticketus actually did, because the IFA has, on more than one occasion, referred to the investment being a loan to the prospective new owner of RFC that allowed him to proceed with his purchase of the club. From my own research it appears that the money was used by the new owner in relation to his purchase of the club. But I think it is clear that Ticketus didn't loan money to him and that the agreement it had was for the purchase of future tickets.

Mr M has said that he was staggered when he became aware that such a significant investment was made by Octopus based on a personal guarantee from the new owner. But the personal guarantee was only one part of the steps that Octopus took in relation to the investment.

Before Octopus's Investment Committee approved the investment by Ticketus the new owner had to provide answers to a questionnaire it provided to him which asked various questions. These included whether he had previously been disqualified as a Director of a company and whether he had ever been accused of fraud or other misconduct in relation to a company or other business.

The new owner answered no to both questions. This was untrue as he had been the subject of proceedings for misfeasance in relation to a company he was involved with and had been disqualified as a Director in 2000 for a period of seven years. I don't think this information was publicly available, so was not something that Octopus could've found out other than by asking the new owner questions.

As well as the questionnaire the new owner was asked to provide a net asset statement which he did. This showed he had enough assets to cover the investment made by Octopus through Ticketus and the subsequent personal guarantee he was asked to provide for that investment.

As well as the personal guarantee from the new owner Octopus also obtained a guarantee from Wavetower, the company that the new owner set up to purchase RFC, as well as Liberty Capital, another overseas company of the new owner that was involved in the purchase of the club. I accept these companies were linked to the new owner, but Octopus had no reason at the time to question the ability of those companies to make good on the guarantees that had been given.

Octopus also referred in its FRL to other steps it took, including; reviewing business plans with future senior management; reviewing full accounts, forecasts, asset values and squad value - with the annual pre-tax profit before the deal being £4.2 million; the investment committee reviewing the proposal over eight months.

It is possible that further due diligence might have turned something up that could've indicated something was wrong and the investment shouldn't go ahead. But what I am considering is whether Octopus carried out sufficient due diligence, and I'm not satisfied that the overall steps it took fell short of what could reasonably be expected.

I think it is important to remember that Ticketus was not investing in the new owner but in future tickets for RFC. It had no reason to think this would not be successful given it had previously successfully invested in that way – albeit in smaller amounts. It had no reason to think that RFC would go into liquidation with investors being unable to withdraw their money from the investment.

I have considered the fact that RFC also had a potential tax liability to HMRC which had come to light in 2009. Octopus has said it wasn't considered likely this would be payable and I note that RFC won the initial tax tribunal case and subsequent appeal - although it lost the final case before the Supreme Court in 2017. Octopus also points to the guarantees it had which gave it further comfort. In the circumstances, although the tax liability was a potential risk, I don't think this meant the investment was inappropriate or fell outside of Octopus' discretionary management remit.

Mr M complained that Octopus didn't action his request for full withdrawal. But I am satisfied that it was never in a position to do this when he first requested this, or subsequently, given RFC had gone into administration in early 2012 and was placed into liquidation on 31 October 2012. I acknowledge that when the IFA chased up the withdrawal in January 2013, he was told that it was on track to pay out full withdrawals at the end of February. Given RFC was in liquidation at this point this information was wrong but there is nothing to indicate this caused Mr M any loss or any other harm.

Mr M has also complained he has not been kept informed of what Octopus is doing with regard to recovering the money he invested and has heard nothing since 2015. He says he and his IFA have chased for updates.

I have not seen evidence of Mr M or the IFA chasing for information from Octopus which it refused to provide.

I have seen evidence of meetings Octopus had with the IFA in 2016 and 2017. These appear to have been general discussions about various clients the IFA acted for rather than meetings specific to any client. This may explain why the IFA has said he didn't have a meeting with Octopus in relation to Mr M.

In addition to those meetings Octopus has provided six-monthly statements which provide up to date valuations for the outstanding part of his investment.

Octopus has said there are ongoing legal actions for recovery, but it isn't known when or what will be recovered at this time and it wouldn't provide information about this until the actions were concluded.

It isn't clear what further information Mr M thinks Octopus should've provided to him. It is possible that it might have been able to tell him something more about the legal avenues Octopus is going down. But I'm not persuaded it has withheld information from him.

my provisional decision

I don't uphold this complaint for the reasons I have explained.

Philip Gibbons
ombudsman