

complaint

Mr and Mrs C's complaint concerns investment advice they received from W H Ireland Limited ('WHI'). They say:

- WHI did not establish their attitude to risk, or carry out any review of their investment needs.
- They were inexperienced investors and the share purchases WHI made on their behalf were not suitable for them.
- WHI bought shares without their consent and later, when limited discretionary powers were granted, they exceeded these.

background

Mr and Mrs C began using the services of WHI in 1998. The relationship was, until 2007, an advisory only one. In June 2007 WHI requested a limited discretionary authority because it felt that there were times when it could not contact Mr and Mrs C. Mr and Mrs C agreed to this, and the limit over which discretion could be exercised was specified as 15% of the total value of their portfolio.

The investment activity undertaken fell into two main categories – trades made at Mr C's instigation (these were large trades in a handful of FTSE100 shares) or trades made on the basis of WHI's advice (these were mostly trades in the shares of smaller companies). The complaint relates to the latter.

An adjudicator considered Mr and Mrs C's complaint and concluded it should not be upheld. In summary, he said:

- Mr and Mrs C had used WHI for some 15 years and would have been aware of the risks involved in trading on the stock markets.
- On balance, it was not unreasonable to believe that their WHI adviser had become aware of Mr and Mrs C's attitude to risk as Mr C had been trading with WHI for a considerable length of time.
- Mr C had gained good experience of how the markets work and also of the potential losses that could be made.
- There is no evidence to show that Mr and Mrs C challenged any of the share purchases made by WHI.
- There is no evidence that Mr and Mrs C were risk averse investors.

Mr and Mrs C did not accept the adjudicator's view. They appointed a representative to respond on their behalf. In summary the representative said:

- Virtually all of the shares WHI purchased resulted in a complete loss or have no realisable value.
- WHI recklessly purchased shares in volumes far greater than market liquidity would support.

- There was a conflict of interest as WHI or companies associated with it were involved with many of the shares it bought.
- Mr and Mrs C accept responsibility for the investment decisions Mr C made, and these do not form any part of their complaint.
- The relationship with WHI spanned 15 years, during which Mr and Mrs C's circumstances and attitude to risk changed enormously. WHI should have carried out regular reviews.
- Mr and Mrs C had no understanding of the risks involved with the kind of shares WHI purchased.
- All the telephone conversation recordings provided by WHI relate to 2011 and 2012, not earlier when the majority of trading took place.
- Mr and Mrs C were "allocated" a significant amount of shareholdings in obscure companies that they simply did not understand. They were continuously advised that the shares could not be sold.
- The discretionary mandate was intended to be used only when Mr and Mrs C were not available. But, in the event, it was used to exert near total control over Mr and Mrs C's portfolio.

I issued a provisional decision in July 2014. My provisional findings were, in summary:

- The investment activity undertaken by Mr and Mrs C fell into two main categories – investments made on the advice of WHI, and investments made by Mr C. Mr and Mrs C say they accept responsibility for the investments Mr C made, and their complaint only concerns the investments made on the advice of WHI. My consideration was therefore limited to those investments, a list of which had been provided to me by WHI.
- One of Mr and Mrs C's points of complaint was that some of the investments made by WHI were made without their authority, either because they were not asked for their agreement, before WHI had any discretion, or because WHI exceeded its authority, after it had been granted discretion.
- Having considered that point, I was unable to reasonably say that the investments should be unwound or cancelled on that basis. I appreciated that some investments were "allocated" to Mr and Mrs C without prior discussion, but I thought it more likely than not that they did then agree to them. Mr and Mrs C were also sent written confirmations after each investment had been made, and I considered it likely that they would have queried these if they had not agreed to the investment or considered that it had been made without authority. I had not seen any evidence of them having done this.
- But it did not follow that the advice to make the investments was suitable – that was a separate point, and in my view the central one to this complaint. In relation to this, I thought the following needed to be considered:
 - Did Mr and Mrs C understand the risk associated with the investments - were they given adequate risk warnings?

- Did WHI adequately take into account the risk associated with the other investment activity Mr C was undertaking when recommending the investments?
 - Did WHI know enough about Mr and Mrs C's personal and financial circumstances to be able to make a reasonable assessment of suitability?
- The list of investments provided by WHI showed that, with the exception of a few larger company shares (less than 10% of the overall investments made) all its recommendations were high risk investments. They were small company shares, listed on the AIM and PLUS markets, or not listed at all. The list, and the valuation statements provided, also showed that the investments were often of significant size – generally well in excess of what is likely to have been normal market size for shares of this type.
- Mr C's trades were always large short term ones in a handful of large company shares he was following – he usually only held shares of two or three of these companies at any one time, and latterly only traded two banking shares. Some of these trades were funded by his money, and some were leveraged by using an extended settlement period.
- The only fact-find WHI carried out was completed in 1998. This did not record an attitude to risk, and recorded limited information otherwise. There were no other records of any discussions about Mr and Mrs C's personal and financial circumstances, their attitude to risk, or their investment objective. WHI had provided some call recordings, but these relate to the final stage of the relationship – there were no recordings available for the bulk of the relationship.
- I did not think it was reasonable to describe Mr C as a sophisticated investor. He followed a handful of FTSE100 stocks and took large short term positions in them when he thought there was a good prospect of a price rise. I had not seen any evidence of his having experience of other types of investment and, in particular, small company shares which had a very different set of risk factors associated with them. Mrs C appeared to have very limited investment experience of any kind.
- Taking these points into account – and the very high level of risk Mr C was already exposing himself to through his own investment activity – I did not think that WHI should have made the recommendations it did. WHI knew Mr C was taking very high levels of risk through his own investment activity. It did not know whether Mr and Mrs C had any other savings beyond those they held with it, and did not know anything about their financial circumstances otherwise.
- WHI did not therefore know enough about Mr and Mrs C's circumstances and understanding to safely conclude that exposing them to very high levels of risk, on top of the risks Mr C was already taking, was suitable.
- Mr and Mrs C have confirmed they had no investments other than what they held with WHI. So it appears all their investments were exposed to a significant level of risk as a result of WHI's advice.

- I also did not consider that WHI adequately explained the risk associated with its recommendations. It said in letters confirming some of the investments that they were 'high' or 'very high' risk, but I had not seen any evidence of it having explained the specific risk factors associated with the kind of investments it was making. There was no doubt Mr C understood risk insofar as it related to the possibility of a share price falling. But I had not seen sufficient evidence to conclude that Mr and Mrs C understood that the investments WHI was making might suffer a complete capital loss or might not be realisable. Neither of these risk factors was present in the kind of investments Mr C had previously made.

For these reasons, I provisionally concluded that the investment advice WHI gave was unsuitable.

Mr and Mrs C accepted my findings. They however asked that I give consideration to making an award for the fees they would have to pay to their representative. They also expressed concern about how any compensation would be calculated.

WH Ireland did not accept my findings, and made further submissions. It said, in summary:

- Mr and Mrs C were experienced investors, who had traded over many years. In addition to the execution only account held with it, Mr and Mrs C held an execution only Contracts for Difference (CFD) account.
- Mr C actively followed the markets with intelligence and understanding.
- It sent many letters to Mr and Mrs C detailing the trades it had undertaken and providing information on the companies invested in.
- Mr and Mrs C signed and returned 21 letters confirming their acceptance of a high risk investment.
- Mr C undertook very large trades on an execution only basis. His general approach to investment was akin to gambling.
- Mr and Mrs C declared that they had assets in excess of £1m.
- Mr and Mrs C ran two successful building companies – they were not simply a builder and a housewife.
- Mr and Mrs C could have been classed as elective professional clients under the relevant rules.
- Mr and Mrs C were very friendly with its advisor – they met for meals and spent time together on holiday.
- It was concerned I had not been provided with copies of all the telephone recordings (it also provided some further recordings for me to consider).
- Mr C has said he accepts responsibility for all the execution only trades – these should therefore be excluded from consideration.

A request for a hearing was also made – this has been dealt with separately.

my findings

I have reconsidered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

At the outset I will reconfirm that my findings only relate to those investments on which WHI gave advice. It is accepted that Mr C made a number of investments himself, and these are excluded from my consideration. It has been established which investments were made on WHI's advice (it provided a list of these) and my understanding is that is not in dispute.

I made three main points when reaching my provisional conclusions.

The first was that Mr C (who carried out all his and Mrs C's investment business) was not a sophisticated investor. He made some investment decisions himself, but his investment activity was limited to taking large short term positions in a few FTSE100 stocks, based on his view (seemingly derived from media reports) of the prospects for those few stocks.

This second was that WHI knew Mr C was taking very high levels of risk through his own investment activity and did not know enough about Mr and Mrs C's circumstances and understanding to safely conclude that exposing them to very high levels of risk (through its recommendations), on top of the risks Mr C was already taking, was suitable.

The third was that WHI had not adequately explained the risk associated with its recommendations. I had not seen sufficient evidence to conclude that Mr and Mrs C understood that the investments WHI was making might suffer a complete capital loss or might not be realisable.

Having carefully considered the comments made by WHI, I have not been persuaded to depart from these points. My final finding is therefore that the advice WHI gave was unsuitable.

In its response, WHI says that Mr and Mrs C were experienced investors, who accepted the high risk associated with its recommendations, and had an approach that was "akin to gambling".

Mr C did have investment experience (as mentioned, I think Mrs C's involvement in their investment business was limited), but that experience was quite narrow. Mr C followed a few large cap stocks, and took short term "punts" on them. I have not seen any evidence of Mr C or Mrs C having any significant experience of the kind of stocks WHI recommended to them. Those stocks were nearly all very small companies which were listed on AIM or PLUS markets or, in some cases, not listed at all. For the purposes of that kind of investment, Mr and Mrs C were not experienced.

There is no doubt that Mr C was a risk taker, and it is not unreasonable to describe his approach to his own investment as gambling. But it does not follow that WHI had the freedom to recommend to Mr and Mrs C anything it liked, in any quantity.

In the event, in the knowledge that Mr C was taking high amounts of risk when making his own investments, WHI made recommendations that were almost exclusively high risk. It recommended large (often far in excess of what would have been normal market size) investments in small companies which often had a very limited operating history.

WHI has made the point that Mr and Mrs C declared assets in excess of £1m, had run successful building companies and were well known by its advisor. But its advisor having met Mr and Mrs C socially was not enough to meet WHI's obligation to know its customer. WHI is only able to speculate, to an extent, about Cs financial circumstances. It did not know the full detail of their financial circumstances – for example, details of their investments/savings, their income/outgoings or any pension provision that had been made. So how did it know that putting large amounts in high risk small company shares was suitable, particularly given the risks being taken by Mr C otherwise?

Mr and Mrs C have confirmed that all their investments were held with WHI (the remainder of their assets being property). So WHI's advice meant that all their investments were exposed to high levels of risk. I am not persuaded that was suitable.

In relation to the disclosure of risk, WHI says Mr and Mrs C signed a number of letters, which confirmed its recommendations as "high" or "very high" risk. But the letters I have seen do not detail the risk factors – they do not, for example, say that Mr and Mrs C might lose all their invested capital, or that Mr and Mrs C might not be able to easily resell the shares if they wanted to. So I am not persuaded that Mr and Mrs C fully understood the risk they were accepting.

WHI has referred to a CFD trading account opened by Mr C. When opening this account, Mr C confirmed that he had not undertaken trading of this type before. The account also appears to have been run through WHI – some of the call recordings provided talk about trades on "the margin account" and there are discussions about transfers of cash in and out of it. It seems likely that the account was opened to provide an alternative method for Mr C to take short term positions in the stocks he followed. The trade history shows Mr C trading a few large cap stocks in the same way as he had on his WHI account. So, whilst I accept that CFD trading involved significant risks (and risks that differ in some ways from the trading method Mr C had used previously), I am not persuaded that the opening of the CFD account offers evidence of the suitability of the advice given by WHI. If anything, it ought to have given WHI cause to consider the suitability of its continuing to recommend high risk investments.

WHI has said Mr and Mrs C could have been categorised as elective professional clients. I am not persuaded that is the case but, in any event, no such categorisation was made, so this is not in my view a relevant consideration.

WHI has also expressed concern that I have not been provided with all the call recordings it submitted (without explaining what it thinks has been overlooked in these calls). I can confirm that I have been provided with the call recordings, and the ones it provided with its response to my provisional decision. I have heard nothing in the calls I have listened to which persuades me to depart from my findings.

WHI says it considers I have departed from the law when reaching my findings. It has made reference to the "assessment of the sophistication of clients" and the "duties of a firm undertaking non-discretionary dealing services", but not specified what law it is referring to or how I have departed from it. The references to the "assessment of the sophistication of clients" and the "duties of a firm undertaking non-discretionary dealing services" appear to relate to WHI's regulatory obligations. I can confirm that my decision is based on what I consider to be fair and reasonable in the circumstances, taking into account what was required by the regulations at the time, including WHI's obligation to know its customer and give suitable advice.

The final point I have considered is Mr and Mrs C's request that I make an award for the fees they need to pay to their representative. Our service is free of charge to consumers and provides an informal alternative to going to court. Consumers should not need special expertise or the help of a paid representative to bring their case to us. We judge cases on the facts - not on the way the case is presented. In this case, I am satisfied that Mr and Mrs C could have dealt with the matter themselves, and they were made aware of their right to refer their complaint to us direct. So I do not think it would be appropriate to make an award for the costs Mr and Mrs C have incurred.

fair compensation

To compensate Mr and Mrs C fairly, WHI should put them as close to the position they would probably now be in if they had not been given unsuitable advice.

I think Mr and Mrs C would have invested differently. It is not possible to say *precisely* what they would have done, but I am satisfied that what I set out below is fair and reasonable given Mr and Mrs C's circumstances and objectives when they invested.

what should WHI do?

- Compare the actual performance of the shares Mr and Mrs C purchased on WHI's advice to the return the invested amounts could have obtained using the FTSE All Share (total return) Index as a benchmark
- The compensation payable to Mr and Mrs C is the difference between the *fair value* and the *actual value*. If the *actual value* is greater than the *fair value*, no compensation is payable.
- WHI should also pay Mr and Mrs C any interest, at 8% simple p.a. on any loss from the date of transfer to the date of settlement. Income tax may be payable on the interest awarded.

actual value

This means the realisable value of the shareholdings at the date they were transferred to another broker by Mr and Mrs C.

If the shares were illiquid (that is could not be readily sold on the open market), it may be difficult to work out what the *actual value* was. So, if the shares are still held, the *actual value* should be assumed to be zero. This is provided Mr and Mrs C agree to WHI taking ownership of the shareholding, if it wishes to. If it is not possible for WHI to take ownership, then it may request an undertaking from Mr and Mrs C that they repay to it any amount they may receive from the investment in future. This is subject to the additional requirement detailed below, which will apply if the compensation exceeds £150,000.

If Mr and Mrs C have since been able to sell shares that were illiquid at the time of transfer, they will need to provide details of the sale, and the amounts received will need to be treated as a 'withdrawal, income or other payment', as detailed below.

fair value

This is what the investment in the shares would have been worth at the end date had it produced a return using the benchmark.

additional capital

Any additional sums that Mr and Mrs C paid into the investment should be added to the *fair value* calculation at the point it was actually paid in.

withdrawal, income or other payment

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 WHI 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 and Mrs C wanted capital growth and to invest in individual shares. The FTSE All Share Index is a reasonable measure of how a well-diversified portfolio of shares may have performed.

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 W H Ireland Limited pays the balance.

determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My decision is that W H Ireland Limited should pay the amount produced by that calculation – up to a maximum of £150,000 plus any interest set out above.

WH Ireland Limited should provide details of its calculation to Mr and Mrs C in a clear, simple format.

If W H Ireland Limited does not pay the full fair compensation, then any investment currently illiquid should be retained by Mr and Mrs C. This is until any future benefit that they may receive from the investment together with the compensation paid by W H Ireland Limited (excluding any interest) equates to the full fair compensation as set out above.

W H Ireland Limited may request an undertaking from Mr and Mrs C that either they repay to it any amount they may receive from the investment thereafter or if possible, they transfer the investment at that point.

recommendation: If the amount produced by the calculation of fair compensation exceeds £150,000, I recommend that W H Ireland Limited pays Mr and Mrs C the balance plus any interest on the balance as set out above.

This recommendation is not part of my determination or award. It does not bind W H Ireland Limited. It is unlikely that Mr and Mrs C can accept my decision and go to court to ask for the balance. Mr and Mrs C may want to consider getting independent legal advice before deciding whether to accept this decision.

John Pattinson
ombudsman