complaint

Mr W complains about Business Loan Network Limited (trading as ThinCats.com) failing to present accurate information on several loans he invested in on its peer to peer lending platform.

background

ThinCats is a peer to peer internet-based lending platform where a group of individual lenders contribute towards a larger aggregate loan to a single borrower. The loans are auctioned so that individual lenders can participate and make a bid. Once a bid is made, the specified amount of money from the member account will be allocated to that bid. Once the borrower accepts enough bids to meet its aggregate lending requirement, ThinCats enter into a loan agreement with the borrower on behalf of all the lenders.

Mr W made a number of investments through his personal account in several loans on ThinCats' platform. He invested a total of £38,000 in three companies owned by the same director. For the purpose of this decision, I've referred to the borrower companies as Company A, B and C. Mr W's investments were as follows:

Company A

In tranche one of this loan Mr W bid £3,000 at a time to make a total of £9,000 in February 2016. Company A sought a total loan of £180,000 for a 12-month term. It had a fixed interest rate of 11.75% with a loan to value of 52%.

In tranche two of this loan Mr W bid £5,000 and then a further £3,000 in February 2016. Company A was seeking to borrow a further £170,000 for a 12-month term. It had a fixed interest rate of 11.25% with a loan to value of 0-30%.

In tranche three of this loan Mr W bid £3,000 and then a further £1,000 in February 2016. Company A was seeking to borrow an additional £170,000 for a 12-month term. It had a fixed interest rate of 13.50% with a loan to value of 30%-60%.

The purpose of all three loan tranches was for *"development finance to allow for capital works, asset purchase and exit through sale".*

All three loan tranches detailed that the security entailed a first fixed and floating charge over the company, a first legal charge over freehold land and buildings, intercompany guarantees from all associated businesses and a personal guarantee from the company director. The director's personal assets were detailed as the following:

- assets with their partner of around £10 million of which £5 million related to their principal residence plus other investment land/properties;
- family trust with further assets of around £3 million which included land and shares in its parent company;
- bank liabilities of £1.7 million;
- after liabilities, without taking into account joint assets or the trust, the director owned in their own right around £3.5 million.

The information pack also set out the fallback and recovery process as follows:

"The subject of what would happen in the event of a distressed situation is something both the Sponsor and the Borrower have discussed in detail.

Regular monitoring enhanced by communication from the borrower and his professionals are the first element of monitoring regarding performance and stress.

- *That in respect of this development the first position is exit by sale. Should that not be achieved then this would revert to refinance with the agreed facility from the issuing Bank.*
- *For whatever reason should this fail then arrangements would be made with for either a Group internal purchase.*
- *Should that fail then an external lending product would be sought.*
- *Should that fail then the assets due to the combined LTV could be sold at auction*
- *Should that fail then inter group funds would have to cover that position.*
- *Should that fail then the shareholding trust and the guarantor would be required to perform.*
- *There are significant layers of fallback positions so as to protects lenders interests.*

Reputationally the Company due to its close associations with the Group and its professional relationships it would be highly undesirable for the Company to fail and so there are considerable safeguards put in place to cover this position."

Company B

In tranche two of this loan Mr W bid £8,000 in April 2016. Company B was seeking £225,000 for a 30-month term with a fixed interest rate of 13.45%. The information showed combined security (taking into account previous loans) of £1,086 million, giving a loan to value of 44%. In addition, the property/business being acquired achieved an annual income of around £60,000.

The purpose of this loan was for commercial investment and capital raising for capital expenditure. The security entailed a first fixed and floating charge over the company, a first legal charge over freehold land and buildings, first charge over new assets acquired and a personal guarantee from the company director.

The director's personal assets, and the fallback and recovery process were the same as that listed above, under Company A.

Company C

In tranche one of this loan Mr W bid £2,000 and then a further £2,000 in December 2016. Company C sought £400,000 for a 14-month term with an interest rate of 11.5%.

In tranche two of this loan Mr W bid £2,000 and then a further £3,000 in December 2016. Company C sought to borrow a further £500,000 for an 18-month term with an interest rate of 12%.

The purpose of both loan tranches was to repay existing loans and for the development of a project and had a loan to value of 62%. The security for both loan tranches entailed a first debenture over the company (all loans ranked equally), omnibus guarantee from all group companies, first legal charge over the portfolio of property with an OMV of £3,335,000 and a personal guarantee from the director for the full amount.

In May 2018 Company A, B and C went into administration and the director was made bankrupt in July 2018, as a result Mr W complained to ThinCats.

Mr W says he made investments in these loans because of the securities that were in place. In particular, the first charge/debenture on the loans and the relatively low loan to values, attracted him to invest. He also says the valuations were completed by quantity surveyors. So, taking all of this into account, he had felt confident that he would have been able to recover his capital, if the market crashed. Mr W says ThinCats has been negligent in failing to provide accurate disclosure and has mis-led investors as the quality of the loans were overstated. Mr W would like ThinCats to return his investment funds in full and pay interest.

ThinCats says it's pursuing claims against third parties with regards to their conduct, including the sponsors who provided information and made representations in the information packs. As part of the initial review, ThinCats identified a limited number of cases where the loans had not received the benefit of the security set out in the relevant information packs and ThinCats had purchased those loans.

One of our investigators looked into Mr W's concerns, and thought Mr W wasn't provided with clear, fair and not misleading information about the loans. She thought it was likely that if Mr W had been provided with clear and accurate information, he wouldn't have invested in these loans. Her reasons were as follows:

- based on the information packs for each loan, Mr W would've been under the impression that any risk he was taking was mitigated by the security it had in place and the prepared strategy to protect him;
- the reasonably low loan to value figures suggested that should the worst happen, Mr W had a good chance of recuperating the funds he had invested;
- ThinCats had a responsibility to ensure the information presented was reliable and not mis-leading. ThinCats hadn't provided evidence of the due diligence checks it carried out;
- whilst the terms and conditions set out that lenders were also responsible for undertaking their own due diligence checks and seeking independent investment advice where necessary, ThinCats needed to comply with the rules set out by the Financial Conduct Authority (FCA);
- ThinCats pursuing the sponsors suggests it acknowledges the checks carried out were negligent;
- if the security described in the information packs had been in place than it's more likely than not the capital invested by lenders would be returned to them.

Our investigator thought Mr W wanted to invest in peer to peer loans, so it was likely that he would have still invested in similar loans in any event and probably would have re-invested in these funds had the loans been repaid by the end of their term. To put things right, she thought ThinCats should:

- calculate how much Mr W received back from his initial investment, including any funds that have been recovered and returned to him;
- then calculate how much Mr W would've received had he received an average rate of return for the loans of similar risk across the platform from the date of investment until the date of settlement;
- if the second was greater than the first then ThinCats should pay Mr W the difference;
- if the first was greater than the second then Mr W hadn't suffered a financial loss so no compensation was payable;
- if recovery was ongoing at the date of settlement, ThinCats should take ownership of the loans. If that was not possible, then ThinCats could request an undertaking from Mr W that he should repay ThinCats any amount he may receive from the recovery distributions in the future.

Mr W accepted. He raised concern that ThinCats had introduced its own star rating on later loans. Mr W asserted that if ThinCats hadn't completed due diligence checks then it shouldn't be making such ratings.

ThinCats disagreed with the view. In summary, it said:

- each loan should be considered on a case by case basis taking into account the platform's terms and conditions at the time of investment, the specific information made available to the lenders, the due diligence under taken by the lender, the time Mr W made the bid on the loan and whether it was purchased on the primary or secondary market;
- whilst security is offered, it can depreciate and dissipate in value;
- terms and conditions made it clear ThinCats did not have a responsibility to verify all the information contained within the loan proposals provided by the sponsor and borrower. All valuations and supporting documents were provided by the sponsor and borrower from third party experts such as solicitors and valuers, so ThinCats was entitled to rely upon them and had not failed in any duty to the lenders;
- there was a time lapse between a loan proposal placed on the platform and an auction starting as lenders were required to carry out their own due diligence and the platform offered a Q&A facility so all potential investors could ask questions or request for more information from the borrower and sponsor;
- ThinCats had brought claims against the third parties as each lender could not bring proceedings individually, this did not amount to a concession of negligence;
- ThinCats' terms conditions set out the risk warnings, an explanation of the secondary market and the role of the security trustee and agent;
- ThinCats has always acted in accordance with the agreed terms and conditions and acted with due skill, care and attention. The ongoing recovery process at its own cost demonstrates it is fulfilling its duty to its lenders as lender agent and security trustee;

- ThinCats doesn't agree with the redress proposal as it doesn't take into account the lenders requirement of completing their own due diligence, understanding of the risk of lending, secured or otherwise. ThinCats should not take ownership of the loans during the recovery process as lenders are made aware in the terms and conditions that the lender makes an individual loan to the borrower.

Our investigator clarified her view and said that the obligation to provide clear, fair and not misleading information about the loans rested with ThinCats. Whilst their terms and conditions suggested that an investor should carry out their own checks, this didn't change the regulatory obligation on ThinCats. And whilst it was open to ThinCats to delegate the checks to a sponsor and third party, ultimately, they remained responsible if the information obtained and then held as being reliable, turned out to be misleading or inaccurate. Investors needed to be in a position to make an informed decision as to risk. The 2018 FCA consultation paper simply clarified how the rules that were already in existence, ought to be interpreted for peer to peer lending.

ThinCats maintains that it was reasonable to undertake a plausibility check, in which it relied upon valuations which appeared to have been prepared by RICS registered valuers. It says there was nothing to suggest that there was an issue with the veracity of these documents at the time. ThinCats says it relied upon due diligence checks being undertaken by sponsor.

As the parties do not agree, the matter has come to me for a final decision.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. Having done so, I intend to uphold Mr W's complaint.

In reaching my conclusions on this complaint, I've taken into account the wider obligations on ThinCats. This includes good industry practice, and any applicable guidance or rules from the FCA.

At the time of promoting Company A, B and C's investment opportunity, ThinCats was authorised and regulated by the FCA. The relevant rules and regulations FCA regulated firms are required to follow are set out in the FCA's Handbook of rules and guidance.

The FCA Principles for Business ("PRIN") set out the overarching requirements which all *whole or in part to every firm".* The Principles themselves are set out in PRIN 2.1.1R. The most relevant principles here are:

- PRIN 2.1.1R (2) *"A firm must conduct its business with due skill, care and diligence."*

- PRIN 2.1.1R (6) *"A firm must pay due regard to the interests of its customers and treat them fairly."*

- PRIN 2.1.1R (7) *"A firm must pay due regard to the information needs of its clients and communicate information to them in a way which is clear, fair and not misleading."*

ThinCats was also required to act in accordance with the rules set out in the Conduct of Business Sourcebook (COBS). And the most relevant obligations here are:

- COBS 2.1.1R (1) *"A firm must act honestly, fairly and professionally in accordance with the best interests of its client."*

- COBS 4.2.1R (1) *"A firm must ensure that a communication or a financial promotion is fair, clear and not misleading."*

So before holding out the promotional material provided by Company A, B and C, ThinCats needed to satisfy itself that the material itself was clear, fair and not misleading. And it also needed to be satisfied that by approving the promotion and allowing its customers to invest in Company A, B and C it would continue to be acting in its client's best interests. It's not disputed that ThinCats did not provide investment advice.

I've looked at the terms and conditions which applied at the time Mr W invested, these are dated 30 September 2015. Under Section 21 Liability it states:

"2. We will use all reasonable endeavours to provide BLN's services with reasonable care and skill and to seek ways in which the risks can be minimised.

3. We will take care to ensure that our communications are clear, fair and not misleading."

This express recognition within the terms and conditions, shows that Thincats was aware of the requirements around information provision.

These terms and conditions did not expressly state that it was for the lender to undertake their own due diligence. But I've seen the statement at page 1 of the terms and conditions document, which says, *"Since investors are making their own decisions they have only themselves to blame for those decisions."* In other words, ThinCats thought it was for Mr W to satisfy himself that the investments were right for him. ThinCats set out risk warnings, an explanation of the secondary market and the role of the security trustee and agent in its terms and conditions.

For investments after 26 February 2016, ThinCats rely upon different terms and conditions, particularly sections 4.7 and 10.10, which expressly state that whilst ThinCats would take "*reasonable efforts to review*" each information pack, it relied upon the information provided by the sponsor and borrower and could not vouch for the accuracy of the information provided. ThinCats relied, "*upon the information by the borrower and sponsor as to the accuracy, fairness, truth, completeness and non-misleading character of the details contained in the information pack."*

It was open to ThinCats to present the information provided from the sponsor to investors for their consideration and it's fair to say that as no advice was being given, it was for each investor to decide whether or to the investment was suitable for them. But it was for ThinCats to undertake due diligence checks on the promotional information to be satisfied that the information being presented on its platform was clear, fair and not misleading, to enable investors to make an informed decision. ThinCats repeatedly says the due diligence checks were down to the investor, but this evidences a fundamental misunderstanding of its responsibilities. And it isn't fair and reasonable for ThinCats to try to exclude their regulatory responsibilities under the later terms and conditions.

ThinCats also say it was “entirely reasonable” to “assume” everything was in order from the face of the documents provided. At its highest, it’s said it undertook a plausibility check, relying upon the valuations allegedly prepared by a RICS registered valuer. Further that it was for investors to put questions to the sponsor through the platform. I don’t think simply looking at the face of a document that was central to the reliability of the security for the loans was enough. In the applicable terms and conditions from 2015 ThinCats held itself out as “*being unusual as it only makes secured loans*”; it was not unreasonable to expect that it would check whether the loans were indeed secured, otherwise the whole premise on which investments were made would have been misleading.

There’s nothing prescribed by the FCA as to what reasonable checks might involve and I agree that reasonable checks vary according to the particular circumstances. But, despite reasonable requests, there’s nothing to show that ThinCats undertook any other checks or steps to satisfy itself of the fair, clear and not misleading nature of the claims or assertions made in the promotional material. It was an obvious risk that if the information was inaccurate, investors would be unable to make an informed decision about the level of risk they would be exposed to when choosing whether to invest. Further, the sponsor was paid by the borrower, so due diligence checks were a common-sense step to minimise the risk of misleading information being shared and to maintain transparency.

I’ve also borne in mind that the FCA said the following in its July 2018 consultation paper on loan-based (‘peer-to-peer’) and investment-based crowdfunding platforms:

“It is our view that it will be unlikely that a platform could argue that it has met its obligations under Principle 2, Principle 6 (PRIN 2.1.1R) and the client’s best interests rule (COBS 2.1.1R), if it has not undertaken enough due diligence to satisfy itself on the essential information on which any communication or promotion is based.”

Whilst ThinCats are right to say that Mr W invested prior to the publication of the consultation paper, I don’t think that makes a material different. The paper simply clarifies the interpretation and application of the rules and guidance which were already applicable to ThinCats at the time. And I’m mindful that the 2013 consultation on crowdfunding also highlighted that investors should be provided with clear, fair and not misleading information so as to be able to make informed decisions. The importance of disclosure was highlighted, namely, that it should be clear to investors how much due diligence had been conducted.

In this case, the information packs about the loans for the various companies, listed several securities as well as the loan to value for each loan. ThinCats now admit that, as part of the process of defaulting the loans, the value of the securities had diminished or were likely over-inflated at the time the loans were promoted to lenders. ThinCats refer to a “dichotomy” between the valuations stated in the valuations provided by the sponsor and the borrower. Further, ThinCats say generally that other details were mispresented in the information packs and in responses to lenders on the platform, including provision of misleading information on the platform about the security ranking of some of the loans. I also note that ThinCats took over other loans where securities weren’t in place at all. The misrepresentations have formed the basis of claims now being pursued against the third parties.

In the absence of any supporting evidence from ThinCats at all, I'm not satisfied on the balance of probabilities that reasonable checks were carried out about the accuracy and reliability of information provided about these loans. I think it is more likely than not that appropriately detailed checks would've identified issues before the promotions were approved. I also think that's a reasonable inference to draw given the lack of information from ThinCats coupled with the admission that all of the companies went into administration by May 2018, following an earlier inability meet the capital and interest repayments from May 2017.

I can't say whether ThinCats would have granted approval for Company A, B and C's loans to be published on its platform, if such checks had been performed. But even if it had decided to approve the loans, despite what it found, ThinCats would have been obliged to share accurate information with prospective investors under the requirement to provide clear, fair and not misleading information.

Mr W has consistently explained that he relied upon the information provided and had wanted to invest in secured loans with a loan to value of around 45%-65%. So, I consider it is likely that Mr W would not have invested had some of these securities and/or loan to values not been as stated, as he'd have been exposed to more risk than he wanted to take.

It may be that ThinCats has subsequently taken advice and legal action to try and maximise returns for the lenders after the loans defaulted. But these steps occurred after the information had been relied upon and the investments had been made, so they can't cure the original shortcomings by ThinCats.

For these reasons, I uphold Mr W's complaint. I consider that it is fair and reasonable for ThinCats to put things right.

putting things right

When looking to put things right for Mr W, my aim is to put him as close as possible to the position he would've been in but for ThinCats' error.

As I've said above, I'm satisfied Mr W wouldn't have gone ahead with his investment. But I do think that Mr W wanted to invest in peer to peer lending. So, if not in these particular loans, I'm satisfied Mr W would've still invested in similar loans if he'd had the chance. I'm bolstered in that view, by Mr W's concession that he holds like investments (which have not lost capital).

Mr W had invested in several loans at different times, so I think he would've probably re-invested his funds had the loans been repaid by the end of their terms.

So, to put him back in the position he would've been in had things not gone wrong, I think that ThinCats should calculate how much Mr W has received back from his initial investment – including any funds that have been recovered and returned to him (A) – the actual value.

It should then calculate how much Mr W would've received, had he received an average net rate of return for loans across the platform from the date of investment until the date of settlement. (B) – the fair value.

If B is greater than A, ThinCats should pay Mr W the difference. If A is greater than B, then Mr W hasn't suffered a financial loss and there will be no financial compensation to pay.

If recovery actions are still ongoing at the date of settlement, and provided Mr W agrees to the redress I've proposed, ThinCats should take ownership of the loans.

If it is not possible for ThinCats to take ownership, then it may request an undertaking from Mr W that he repays any amount he may receive from the recovery distributions in the future. It wouldn't be fair for Mr W to benefit from any future payments received from the loans when he's already been compensated.

my final decision

For the reasons given, I am upholding this complaint. I direct Business Loans Network Limited to put things right as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 4 April 2021.

Sarah Tozzi
ombudsman