

## The complaint

Mr A complains he was incorrectly categorised as an elective professional client (EPC) by IG Index Limited, which led to him incurring significant losses on his CFD trading account.

## What happened

Mr A originally opened an account with IG as a retail client in 2010. He opened a further account in 2014 on which he then traded reasonably regularly until 2020.

In August 2020, following a short period of particularly high-volume trading, he spoke with IG as he felt he was paying too much in commission and wanted to negotiate a better rate. As a result of this interaction, he was recategorised as an EPC and his commission rate was reduced.

He then continued to trade for several months, until November 2020, during which period he incurred significant losses. Soon after, in March 2021, his representatives complained to IG that he'd been wrongly recategorised as an EPC.

IG didn't uphold the complaint. It said it had followed the correct procedure and it had been reasonable for it to conclude that Mr A met the criteria needed to be recategorised and treated as an EPC.

The complaint was then referred to this service where our investigator concluded it should be upheld. In brief, he felt IG had failed to evidence that Mr A had met the criteria, so had incorrectly recategorised him. The investigator proposed that IG rework the trades Mr A had placed after he was recategorised as if he had remained as a retail client and pay any difference in the amount of loss incurred, plus interest.

IG didn't accept the investigator's view. It felt he'd misapplied the relevant regulation and guidance in reaching his conclusions. It remained of the view that it had acted correctly and reasonably in dealing with Mr A's recategorisation.

As no agreement could be reached, the matter was referred to me to review.

I issued a provisional decision in which I said, in part:

*"Before I look in detail at the administrative process followed by IG in recategorising Mr A as an EPC, I think it's important to look at how the recategorisation first came about.*

*Around the 5/6 August 2020 there were a series of telephone calls between Mr A and member of staff at IG, who'll I'll refer to as X. It's not entirely clear what first prompted the interaction, but what is clear is that the interaction developed into a discussion about Mr A's concerns with the level of commission he was paying to IG. He made clear that if IG couldn't improve upon the rates it was offering, he would move to another provider.*

*Following an amicable discussion about various investment related issues – hedging, etc – and Mr M's plans to become a full-time trader, X raised the subject of Mr A's account status. She explained that there was nothing IG could offer Mr A in respect of a commission*

*reduction as a retail client, but that it sounded like he might qualify as a professional client. And if he became one, IG could consider a rebate or discounted commission.*

*Mr A response to this was that IG should “put me on this professional fees straightaway and I’ll monitor you” and if he was happy with the service, he would remain a client.*

*X explained that the change couldn’t be done immediately and stressed that there was an application process that would need to be completed. She also highlighted at this point that recategorisation as an EPC would involve the loss of the Negative Balance Protection (NBR) afforded to retail clients, which Mr A noted but said wasn’t an issue as he had back-up finance.*

*There was then a discussion of the EPC criteria and X explained one of the requirements, that Mr A demonstrate he had a savings and investments portfolio valued in excess of €500,000. He highlighted the sum on held on his IG account at that point, which was around £370,000 (circa €440,000), but, as this didn’t meet the requirement, X stressed the need for Mr A to provide screenshots or statements demonstrating his overall portfolio to be in excess of €500,000. He confirmed he’d be able to provide whatever was required.*

*There then followed a call during which X helped Mr A though the on-line application process. Mr A appeared to be unsure as to what options to select and was guided by X. For instance, for the question relating to the number of significantly sized trades he’d placed on average per quarter over the last year (one of the other EPC criteria), she guided him to the ‘30+’ option. She also guided him to select the option for the current value of his savings and investments as ‘£500k - £1m’.*

*Shortly after, X called Mr A to tell him that his application had been approved. He was grateful and questioned whether it had happened so quickly because of his lengthy trading history with IG. X said yes but added that she also asked someone for a favour. On a further call soon after, X confirmed to Mr A that his commission rates would be reduced by 30%, on the proviso that he maintained his recent level of trading.”*

I then went on to explain that I’d given this high level of background detail as I thought it provided important context to the matter. I felt it suggested that Mr A’s categorisation had come about solely as a result of his desire to obtain lower charges and wasn’t something he’d initiated. I also questioned whether Mr A was likely to have been aware of the EPC status prior to the interaction.

I thought all this was significant in light of the guidance issued by the European Securities and Markets Authority (ESMA) in 2018, which had indicated that a request for recategorisation should be at the consumer’s own initiative. And, further, that firms should refrain from incentivisation and inducement. I was concerned that Mr A’s recategorisation hadn’t been at his own initiative and that he’d been incentivised by the possibility of obtaining lower fees.

That said, I acknowledged that X had reason to think Mr A might qualify to be recategorised, had warned him of the loss of NBP and that overall, this didn’t appear to be an example of a ‘hard sell’. But I nevertheless didn’t feel the circumstances taken in the round sat comfortably with the rules at COBS 3.5.3, and particularly the ESMA guidance.

My provisional decision then went on to look in more detail at the application process. In this respect I said, in part:

*“Turning then to the application process itself, the investigator’s view focussed on the requirements at COBS 3.5.3. Specifically, he was concerned that IG had failed to ensure that as part of its assessment of Mr A he met two of the three COBS criteria -*

*(a) the client has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;*

*(b) the size of the client's financial instrument portfolio, defined as including cash deposits and financial instruments, exceeds EUR 500,000;*

*(There is a third criterion concerning professional trading experience, but Mr A confirmed he had none, so it’s not relevant here.)*

*Looking first at (b), as noted, it was acknowledged during the initial discussions between Mr A and X that he would need to demonstrate that his portfolio was of the relevant size as he didn’t quite have that amount held with IG. He made a several comments that indicated his portfolio was of the relevant size – for instance that he was planning to invest £1million with IG – but no supporting documentation was ever forthcoming, primarily because it was never sought by IG, it instead being satisfied the criterion was met based on a combination of what Mr A had said and the amount of money he held with IG.*

*In this respect IG was effectively allowing Mr A to self-certify that he met the criterion. It was IG’s actions in doing so that the investigator questioned, and which formed the basis of his conclusion that it had acted incorrectly. He quoted the ESMA guidance previously noted above in concluding that IG was wrong to rely on self-certification.*

*IG has challenged this interpretation of the regulations and guidance. And I think it makes a fair point in this respect. The ESMA guidance says “Whilst investment firms should use their discretion to determine the reasonable steps needed, they should avoid relying solely on self-certification by the client (my emphasis) and should consider obtaining further evidence to support assertions that the client meets the identification criteria at that point in time, notably when they consider that the documents or statements received from the clients are not sufficiently conclusive.”*

*So, I think it would be reasonable for IG to argue that, in taking into account the €440,000 Mr A held with it in conjunction with his comments about the overall amount to he had to invest (and with his comments about his wider business interests) it was carrying out an adequate assessment that gave it reasonable assurance (to use wording that reflects that found at COBS 3.5.3 and 3.5.6) that Mr A met the criterion.*

*But that said, I’m not so sure that this type of reasoning can also be applied to IG’s consideration of the other criterion at 3.5.3 (2) (a), regarding Mr A’s trading history. As noted, for the question relating to the number of significantly sized trades he’d placed on average per quarter over the last year, X guided him to the ‘30+’ option. It appears she was doing so on the basis of Mr A’s trading history for the previous five weeks, during which he placed 194 trades, 117 of which were considered by IG to be significant sized trades.*

*However, prior to this five-week period of intense activity, which had started late June 2020, Mr A had traded only once during the rest of 2020, in March. And before that his last trade was placed on 30 August 2019, around which time he placed five trades, only one of which was of significant size. And prior to that, there was a gap of another five months, going back to March 2019.*

*So, while Mr A had just about averaged 30 significantly sized trades per quarter over the previous four quarters – and therefore in excess of the 10 per quarter as set out in the rule –*

*his activity was actually confined to only the previous quarter. Prior to this he'd placed 85 significantly sized trades in 2019, 24 in 2018, none in 2016 and 2017, 30 in 2015 and 204 in 2014, the year he opened the account.*

*IG has noted that the rule at COBS 3.5.3 (2) (a) makes no requirement that there be a minimum number of transactions in each quarter, simply that the average over the year be 10 per quarter. I appreciate this and agree that if the wording is interpreted too strictly it has the potential to generate some perverse outcomes. Further to the rule itself, the ESMA guidance adds that "Clients who have been trading on the relevant market for less than a year cannot fulfil the conditions... This is because, to assess whether a client meets such conditions, investment firms shall review the client's trading history on the relevant market **over the past four quarters** (my emphasis)."*

*Stepping back from a strict consideration of how the rule is written, I think that a reasonable interpretation of what it (alongside the ESMA guidance) is intended to achieve is to ensure that consumers who are recategorised as EPCs first demonstrate a reasonable volume and consistency of trading over the course of the year prior to the change.*

*I appreciate that in Mr A's case he had been trading for several years, but in the year – the four quarters – immediately preceding his application for recategorisation I don't think he can be said to have demonstrated a volume and consistency of significantly sized transactions. I think it's reasonable to say that he while he clearly had a lengthy overall trading history, his activity preceding the application was effectively limited to only five weeks and, as such, his circumstances didn't really fit with what the regulation is intended to achieve.*

*That all said, in line with my comments regarding to the portfolio size criterion, there might be circumstances in which I'd be persuaded that a consideration of the wider circumstances of Mr A's trading history could form part of an adequate assessment of his knowledge and understanding that gave reasonable assurance if it were the only issue. Perhaps if all other aspects of the recategorisation were consistent with the regulation and guidance.*

*But that isn't the case here. It wasn't solely Mr A's trading history that potentially failed to meet the requirements."*

I then concluded, in summary, that it seemed to me that Mr A had been incentivised by the offer of a better deal on commission, so had not been recategorised as of his own initiative, and further his recategorisation had been on the basis of two criteria, neither of which he strictly met, either in practise and/or in spirit.

I acknowledged again that Mr A had been warned of the loss of NBP and would also have received numerous risk warnings and signed to acknowledge this. But I nevertheless felt unable to conclude that IG had acted fairly as I felt the circumstances strongly suggested that this was the type of situation that the rules and guidance were designed to try to prevent – a consumer being recategorised as a professional client when motivated to adopt that status for potentially misguided reasons and without a solid background supporting it as the right course of action for them.

Mr A's representative confirmed he was in agreement with my provisional decision.

IG provided some further submissions, which are summarised below.

- It was concerned my description of its correspondence with Mr A could be misconstrued as improper conduct. I'd placed weight on the analysis of COBS 3.5.3 (1) relating to the account upgrade that could be seen to restrict firms from balanced discussions of the existence, features, and risks of EPC accounts with potentially eligible clients, unless

they used the specific language of COBS 3.5.3. Given the constraints of communication in COBS 22.5.6 and the intention of COBS 3.5.3 (1), firms were rightly prevented from advertising EPC accounts or incentivising or inducing retail clients to apply. But I'd set an unrealistic expectation that retail clients would need to know the precise language of COBS 3.5 when making an upgrade request, otherwise a firm couldn't satisfy the 'at own initiative test'. This would create unnatural correspondence and frustrate the objectives of clients eligible to apply for features only available in professional accounts.

- The analysis of the 'at own initiative test' in this case should be reviewed within the context of IG's wider control framework, designed to meet the requirements of COBS 22.5.6 and the requirements and spirit of COBS 3.5.3(1). For example, IG has no public-facing marketing about EPCs, no incentives for employees to upgrade accounts and an upgrade process separate to its client relationship managers.
- Mr A initiated the overall correspondence and made clear his objective of lower fees. X confirmed this was only possible as an EPC and explained it couldn't be guaranteed even if his application was successful. Given her warning that an EPC loses consumer protection and her prudent check that Mr A may be eligible to apply based on his account information, IG disagreed this could be construed as inducing or incentivising, or contravened the requirements or intention of COBS 3.5.3.
- The "own initiative" procedure at COBS 3.5.3 (3) (a) requires that "*the client state in writing that they wish to be treated as professional client*". This prevented firms from recategorising retail clients at the firm's own initiative; it wasn't intended to mean that a firm couldn't mention the possibility of reclassification. Within IG's procedure, the request to be treated as an EPC was initiated by a client requesting in writing. So, as a matter of fact, Mr A's application had been at his own initiative. The requirements in COBS 3.5.3 (3) didn't prevent a firm from mentioning that EPC categorisation exists prior to the client's written request. Further, while IG acknowledged the "own initiative" procedure, it was only one part of the process that also required COBS 3.5.3 (1) and, where applicable, 3.5.3 (2) to be satisfied. Recategorisation is a three-step process, and it wouldn't make sense for the "own initiative" procedure to be interpreted such that a firm couldn't even mention that EPC categorisation exists.
- COBS 3.5 is silent on inducements being offered to upgrade but ESMA's guidance suggested firms refrain "*from implementing any form of practice that incentivises, induces or pressures an investor to request to be treated as professional.*" But this guidance concerned providers actively advertising upgrading to retail clients. IG agreed this would be inappropriate. But that didn't happen here. Mr A saw no advertising campaign and promotional language wasn't used when speaking to him. The provisional decision had taken the guidance so far that it was almost impossible for a firm to discuss EPC status at all. This approach was also inconsistent with a 2020 final decision that noted: "*In some cases, the idea of reclassification can indeed be initiated by a firm, for example in the context of the firm taking a view that, based on account activity, the account holder might wish to consider a reclassification*".

IG also made some observations about the calls between X and Mr A. It didn't feel X had initiated the process and she'd only mentioned the EPC upgrade in the context of Mr A's comments about his significant experience and wish to obtain lower fees. Upgrading was the only way this objective could be met so X had to explain this.

X had checked his account details, which had looked likely to meet the criteria. And it seemed he'd already been aware of EPC status as he appeared to know how it worked. X didn't guarantee any reduction in fees and mentioned the loss of NBP. And she hadn't 'guided' Mr A as I'd suggested, rather she'd responded to his request for help and 'played back' to him information already provided. Lastly, my comment regarding X being granted a favour had been taken out of context. It had been a matter of the application being processed promptly, not with any loss of quality or influence on the outcome from X.

## **What I've decided – and why**

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

In doing so, I've taken into account relevant law and regulations; relevant regulators' rules guidance and standards; codes of practice; and, where appropriate, what I consider was good industry practice at the relevant time. But I think it's important to note that while I take all those factors into account, I'm ultimately deciding what I consider to be fair and reasonable in all the circumstances.

Further to the responses to my provisional decision, I remain of the view that the complaint should be upheld, and broadly for the reasons provided in my provisional decision. That said, I think it would be useful to respond briefly to IG's further submissions, particularly in respect of its concerns with my comments about the issue of incentivisation, and the behaviour of X.

My stressing of the incentivisation point was made in the context of the very specific circumstances of Mr A's complaint and the particular way in which I felt he came to be recategorised as an EPC. That being that it stemmed very much from a single objective on his part – wanting to obtain lower fees – as opposed to a more holistic desire to trade in a different way, as a professional.

My intention wasn't to imply that a business cannot in any circumstances bring the potential for EPC recategorisation to a client's attention, particularly where it has good reason to think that client might well meet the required criteria. My point was more that, in light of the regulation and related guidance (and particularly the loss of protections afforded to retail clients) doing so should be handled with caution.

That's not to say that in this case I felt X acted recklessly or personally sought to incentivise or induce Mr A. As I said in my provisional decision, I didn't perceive the situation and the nature of X's communications with Mr A as a 'hard sell' on her part. And I fully acknowledge that she drew attention to the loss of NBP and offered no guarantee that a successful EPC application would see him definitely granted lower fees. And I note and acknowledge what IG has said about it not advertising or promoting EPC recategorisation or incentivising its staff in any way.

To reiterate, my view was more that, in all the circumstances, I felt Mr A's recategorisation was, as I said in my provisional decision, the type of situation that the rules and guidance were intended to try to prevent happening – a consumer being recategorised as a professional client for potentially the wrong reasons and without a clearly demonstrable, robust background that supported it being the right course of action for them. I think it's important to remember that the incentivisation point and more subjective elements of the process aside, as of the date of his recategorisation Mr A didn't meet, or hadn't fully demonstrated that he met, the requirements of the quantitative test at COBS 3.5.3 (2).

I accept this is a finely balanced matter. Mr A was an experienced trader and clearly did actively engage with the process. But in all the circumstances, I find I remain of the view that he shouldn't have been recategorised as an EPC.

## **Putting things right**

Mr A should be put in the position he'd have been in if he hadn't been recategorised as an EPC in August 2020. I'm satisfied he would most likely still have placed the same trades that he placed as an EPC if he'd remained as a retail client, but with the different margin

requirements and protections afforded to retail clients.

As such, IG should rework the trades placed after Mr A was categorised as an EPC as if he'd remained categorised as a retail client, using the relevant rules and margin requirements that were in place at the time. It should then compare the total Mr A would've lost as a retail client to what he lost as an EPC and pay him the difference, plus 8% simple interest from when he stopped trading to the date of settlement.

I consider this to be a fair and reasonable way in which to put things right. Mr A's activity prior to the conversations of 5/6 August 2020, and the content of those conversations, suggest he would most likely still have continued trading in a similar vein if he'd not been reclassified. So, for clarity, it's not *all* his losses incurred between 6 August 2020 and the end of November 2020 that should be refunded, but any *additional* losses incurred by virtue of him being treated as an EPC.

### **My final decision**

For the reasons given, my final decision is that I uphold the complaint and direct IG Index Limited to pay compensation to Mr A as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 12 April 2024.

James Harris  
**Ombudsman**