DRN-4667059

The complaint

Mr P's complaint is about his Capital Com (UK) Limited ('Capital') trading account for Contracts For Differences ('CFDs') and Spread-betting.

He says Capital is responsible for his trading losses, in what he considers to have been an inappropriate high-risk, leverage-based trading account. He claims Capital failed in its duty to protect him from the accumulation of the losses, and he believes it was probably unauthorised to issue the account to him, at the outset, in his offshore home jurisdiction.

Capital disputes the complaint. It says Mr P passed the appropriateness assessment for the account, that he satisfied its source of fund assessment, that he was given relevant risk warnings and that it had no restrictions with regards to onboarding clients from his home jurisdiction.

What happened

One of our investigators looked into the complaint and concluded it should not be upheld.

Mr P disputed this outcome and his case was referred to an Ombudsman – to me. On 21 February 2024 I issued a Provisional Decision ('PD') for the complaint, in which I upheld it.

The PD summarised the investigator's findings and the background mainly as follows –

"*He referred to Mr P's application for the account in January 2021 and the appropriateness questionnaire he completed.*

In terms of his profile at the time of the application, the investigator noted that the questionnaire responses confirmed Mr P was unemployed, was not educated beyond Secondary School level, had annual income below £25,000, sought to invest between £1,000 and £50,000 over the long term, estimated his wealth between £25,000 and £50,000, had no trading experience (in the products within the account, and in the previous three years), and was aware of the risk of losing money in speculative investments.

According to Capital's scoring matrix, Mr P passed the assessment. The investigator also noted that he was granted the trading account after accepting Capital's Risk Disclosure Statement ('RDS').

The investigator considered correspondence between the parties in which Mr P queried why he had a CFD account when he had expected a stock trading account, in which he queried the workings of the account's leverage settings and in which he questioned the difference in a trade's prices, between the price on the platform and the price in the underlying market.

Consideration was also given to his trading losses.

However, overall, the investigator concluded with the following main findings:

- *Even if Mr P did not fully understand the risks at the outset, his trading experiences in*

the account gave him such understanding. With that understanding, given the fact that he did not have an income and the fact that he was incurring losses, he still did not stop trading. A decision to stop trading would have been expected in such circumstances. Instead, he continued to do so, with different outcomes. There is no evidence of any indication from him during this period that could have given cause to Capital to stop his trading.

- *Capital did not provide an advisory service, so it was only obliged to ensure the account was appropriate for Mr P. That required it to satisfy itself that he had the necessary knowledge and experience to understand the risks involved in trading in the account. Some of his questionnaire answers gave cause for thought over whether (or not) the account was one he should open, but his financial and employment circumstances did not automatically mean he could not have a trading account.*

- *On balance, the questionnaire answers are enough to conclude that Mr P understood the risks that would be involved in trading in the account.*

- *Capital's regulatory authority confirms it was authorised to provide services to residents of Mr P's home jurisdiction.*"

"[Mr P] *argued that it is inconceivable to conclude that the account was appropriate for him, in light of his unemployed status and limited financial circumstances; and with proper regard to the facts that he had 'zero' trading experience, no CFD experience, no relevant education, no relevant professional qualifications or work experience, no understanding of how margins worked (and how they increased risk) and had answered only half of the questionnaire correctly.*

He also found it concerning that, despite the complaint and its referral to us and despite his account having previously been suspended (supposedly for his protection), he had recently been invited by Capital to submit identification documentation in order to be allowed to resume trading."

The PD's findings were as follows –

"*Primarily, my provisional conclusions are that the trading account was inappropriate for Mr P, that this was or should have been apparent to Capital at the outset, that he should never have been granted the account and, had that been the case, the subsequent trading events in the account (and their outcomes) would never have happened. For these reasons, I do not consider it necessary, or relevant, to address details of the trading and losses that occurred within the account or Capital's authority to offer its services in Mr P's home jurisdiction. The provisional conclusions are enough, on balance, to determine the complaint.*

Appropriateness, under the regulator's Conduct of Business Sourcebook ('COBS') rules (at COBS 10 and 10A), must be assessed by a firm in order to determine whether (or not) a client has sufficient knowledge and experience to understand the risks involved in the service or product offered by the firm. Such understanding (of associated risks) is commonly expected to come from a client's knowledge, experience and/or familiarity with the relevant service or product itself, and this is reflected in the lines of enquiry that the rules ask firms to apply (as summarised below).

The above is distinct from a firm's duty to provide risk warnings. Risk warnings give information on risks. Appropriateness is the process by which firms must assess whether (or not) a client has enough knowledge and experience to understand such information and to understand the reality of the risks associated with the service or product offered by the firm.

In this respect, and as set out in the rules, the following is important:

- *Information about the type of service(s) and investment product(s) the client is familiar with.*

- *Information about the nature, volume, frequency and length of the client's experience with any such service(s) and investment product(s).*

- *Information about the client's level of education and profession.*

A firm is obliged to warn the client if the assessment concludes that its service or product is inappropriate. If, despite the warning, the client still wishes to proceed with the service or product the firm has discretion to allow the client to do so, "… having regard to the circumstances".

In Mr P's case, it is a matter of fact that Capital concluded, from its appropriateness assessment, that the trading account was appropriate for him. It has repeated this in its complaint response and in its submissions to us. For the reasons I address next, I am persuaded that its assessment and conclusion were flawed.

At the application stage, Capital had enough information from Mr P to know that he had no previous trading experience (certainly none in CFDs), no relevant previous experience of operating a trading account, no trading or investments related education and that he had no reference to a trading or investments related profession. The appropriateness assessment outcome document shows that in response to a question about CFD trading experience he said – "Not at all".

His trading inexperience was also illustrated in the incorrect answers he gave to a couple of the other questions. There was a question about what a 'stop loss order' meant. In reply, he simply said "Yes", which suggests he did not know the answer, otherwise he would have said what he understood a stop loss order meant. A stop loss order is an important and somewhat fundamental risk management tool in trading. It could reasonably be argued that Capital ought to have been alerted by this incorrect answer alone – and certainly in conjunction with everything else I have noted above (and will note below) – to the likelihood that the account was inappropriate for him.

Another question was about who's responsibility it would be to fund an account when its balance falls below the minimum margin requirement. In response, Mr P said "NO". It is reasonable to say this indicated he either could not understand the question or that he understood it but gave the wrong answer. Either way, this ought to have raised another cause for concern in the assessment process.

The document shows that he correctly answered a question about the calculation of margin and that he was aware of the risk of losses in speculative investments, but these do not overshadow or outweigh the overall profile he presented to Capital during the application and assessment stage. That profile being one in which, as I said above and as I quote, "… he had no previous trading experience (certainly none in CFDs), no relevant previous experience of operating a trading account, no trading or investments related education and … no reference to a trading or investments related profession".

In the above context, Capital had essentially no information on the type of service(s) and investment product(s) Mr P was familiar with because he had no history of such familiarity to reference; and it had no information about the nature, volume, frequency and length of his experience with trading or CFD trading because he had no such experience to mention; so Mr P could not meet or pass two of the three key considerations set out in the relevant

appropriateness rules; and the information it had about his education/profession – the third key consideration – was that neither lent itself to compensate for his lack of knowledge, experience and familiarity.

The above analysis shows that Capital's appropriateness assessment of Mr P's application, regardless of whether it was an automated or manual or mixed process, ought to have concluded that the leveraged CFD and Spread-betting trading account was inappropriate for him. His lack of trading knowledge and experience was quickly evident early into his use of the account. The investigator cited some examples of the trading enquiries he put to Capital (as I mentioned in the previous section).

There is correspondence in which he sent a query to Capital about the pricing of a trade. The issue was essentially about the two-way nature of trading quotes, with the buying price higher than the selling price and a spread in between. It appears that he did not know enough (or at all) about this characteristic and was alarmed by its effect on a trade. It also looks like he was unaware of the existence and purpose of a spread, until it was mentioned to him.

There is evidence of another correspondence in which he displayed confusion about the practical workings of leverage in trades, and despite having begun his trading in February 2021 there is evidence of Capital still having to give him basic information about how CFD trading works in April 2021.

I consider the RSD to be irrelevant. As I said above, risk warnings are distinct from the assessment of appropriateness. The former provides disclosure of information on risks and the latter is about assessment of a client's understanding of the reality of those risks (based on a combination of familiarity, knowledge, experience, education, profession).

For the reasons given above, I intend to uphold Mr P's complaint in my final decision if nothing received from the parties in response to this PD alters my findings.

It follows from the above that Mr P should never have been granted the inappropriate trading account. Had that happened, none of the trading that took place in the account would have taken place. The same applies to the outcomes of all those trades, they would not have happened because there would have been no trading in the account, because there would have been no account. Capital holds responsibility for granting him the inappropriate trading account, so its responsibility extends to the events and consequences that flowed from that.

In terms of redress, my provisional conclusion is that Capital is responsible for compensating Mr P for all capital loss he incurred in trading within the account. In the final decision, and if my conclusions in this PD remain unchanged, I will order it to pay him this compensation. He would not have lost any of his capital if he did not have the account and if no such trading happened. I have not seen evidence that he would have opened a comparable account (and traded) elsewhere. Even if Capital argues that he could have done so, it is safe to conclude that any other firm would have been expected to reach the same conclusion that Capital ought to have reached – that a comparable account was inappropriate for him and would not be granted to him.

The above findings also mean that Mr P would probably have used his capital for personal reasons, as opposed to trading, so I provisional find that in addition to compensation for capital loss (as stated above), Mr P must also be compensated for the loss of use of that capital. To achieve this, in the final decision and if my conclusions in this PD remain unchanged, I will order that Capital pay him interest on the capital he lost in the trading account at the rate of 8% simple per year from when each loss was incurred (and for each specific loss amount) up to the date of settlement. In the alternative, and/or if given good

reason by the parties to do so, I could consider the simpler method of applying the same interest to the total capital loss from the last date of all Mr P's losses to the date of settlement.

In the final decision, I also intend to order Capital to pay Mr P £300 for the trouble and upset the matter has caused him to date."

Both parties were invited to comment on the PD. Mr P confirmed that he accepts it.

Capital explained the evidence of the appropriateness questions I referred to in the PD. It acknowledged that the evidence might not have been clear on the specific questions put to and answered by Mr P. It said the actual questions were –

"(1) If you open a £100,000 position with 1:100 leverage, what is your margin?
A: 1000, B: 400, C: 70000

(2) Will a stop loss order limit the negative exposure of your position in a volatile market?
A: Yes, B: No

(3) Will Capital.com add money to your account if your balance falls below the minimum margin amount?
A: Yes, B: No"

It said Mr P answered the questions correctly, which underpinned his passing of the appropriateness test.

Capital accepts that Mr P was inexperienced in trading CFDs, but it argues that his appropriateness test answers demonstrated he understood the fundamentals of leveraged trading and risk management. With regards to his inexperience, it argues that his acceptance of the RSD confirmed he understood the risks associated with trading, and it had no cause to consider otherwise at the point of his onboarding. It also said it would be unreasonable for a firm to reject an application like Mr P's simply on the grounds of the applicant being unemployed.

It requested that the PD be reviewed in light of its comments and that, without acknowledgement of liability, the same should be done to the PD's redress findings.

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.

I have reviewed the complaint and considered Capital's comments. Having done so, and on balance, I am not persuaded to depart from the main conclusions reached in the PD (as quoted above). I retain those conclusions and incorporate them into this decision.

In summary – the CFD trading account gave Mr P access to trading CFDs; CFDs are inherently complex and high-risk products; he presented a profile (as addressed in the PD) at the point of onboarding that, overall, made such an account inappropriate for him; Capital wrongly concluded that the account was appropriate for him and did not warn him that it was not; had he received such a warning, I have not seen evidence to suggest he would have proceeded with the account regardless; and had Capital declined his application, he could not have proceeded with the account.

Capital's responsibility to assess and determine appropriateness of the account for Mr P was

especially triggered by the complex and high-risk nature of CFDs – CFDs being one of the derivatives covered by COBS 10. It says it applied the assessment and I accept that it did, the PD did not say otherwise, but, on balance, the outcome of its assessment was wrong.

I appreciate the explanation Capital has given about the test questions, but I must acknowledge that the full questions quoted above are as it has presently described. I have not seen evidence that they were within the test Mr P undertook at the relevant time, but I also acknowledge that I have no cause to doubt Capital's explanation. Nevertheless, and due to the lack of such evidence, it is possible he might dispute the questions. In any case, I have not sought to determine their accuracy any further because the complaint does not turn on them.

As I addressed in the PD, it is mainly the mismatch between the account and Mr P's profile (at the point of onboarding) that matters. In this respect, the following findings from the PD still stand –

"*At the application stage, Capital had enough information from Mr P to know that he had no previous trading experience (certainly none in CFDs), no relevant previous experience of operating a trading account, no trading or investments related education and that he had no reference to a trading or investments related profession. The appropriateness assessment outcome document shows that in response to a question about CFD trading experience he said – "Not at all".*"

"… *Capital had essentially no information on the type of service(s) and investment product(s) Mr P was familiar with because he had no history of such familiarity to reference; and it had no information about the nature, volume, frequency and length of his experience with trading or CFD trading because he had no such experience to mention; so Mr P could not meet or pass two of the three key considerations set out in the relevant appropriateness rules; and the information it had about his education/profession – the third key consideration – was that neither lent itself to compensate for his lack of knowledge, experience and familiarity.*"

With regards to the RSD, nothing Capital has said in its comments defeats the following finding in the PD –

"*I consider the RSD to be irrelevant. As I said above, risk warnings are distinct from the assessment of appropriateness. The former provides disclosure of information on risks and the latter is about assessment of a client's understanding of the reality of those risks (based on a combination of familiarity, knowledge, experience, education, profession).*" [my emphasis]

Mr P's stark inexperience was an ever-present context for the entire assessment and that applied to him accepting the RSD too. He did not have the trading familiarity, knowledge and/or experience to understand the reality of the risks he was undertaking by doing so, and by acquiring the CFD trading account.

I appreciate that the evidence of correspondence between the parties that I mentioned in the PD is from the period after the assessment of appropriateness (and his onboarding) had concluded. However, they happened quite shortly thereafter and they give an insight into how unaware Mr P was, early in his operation of the account, about what he had entered into.

As I said in the PD, our investigator mentioned "… *correspondence between the parties in which Mr P queried why he had a CFD account when he had expected a stock trading account, in which he queried the workings of the account's leverage settings and in which he questioned the difference in a trade's prices, between the price on the platform and the price*

in the underlying market."

The PD then noted as follows –

"*There is correspondence in which he sent a query to Capital about the pricing of a trade. The issue was essentially about the two-way nature of trading quotes, with the buying price higher than the selling price and a spread in between. It appears that he did not know enough (or at all) about this characteristic and was alarmed by its effect on a trade. It also looks like he was unaware of the existence and purpose of a spread, until it was mentioned to him.*

There is evidence of another correspondence in which he displayed confusion about the practical workings of leverage in trades, and despite having begun his trading in February 2021 there is evidence of Capital still having to give him basic information about how CFD trading works in April 2021."

I referred, above, to Capital's comment about Mr P's unemployed status at the time of his application, and I did so in order to reflect the argument it made. However, I do not consider it necessary to address it further because neither the PD's conclusions, nor those in this decision, are based on him being unemployed at the time of his application.

Overall, on balance and for the above reasons (and those in the PD), Mr P's complaint is upheld.

Putting things right

Fair Compensation

My aim is to put Mr P into the position he would probably now be in had he not been granted the inappropriate trading account by Capital. As I said in the PD –

"… *Mr P should never have been granted the inappropriate trading account. Had that happened, none of the trading that took place in the account would have taken place. The same applies to the outcomes of all those trades, they would not have happened because there would have been no trading in the account, because there would have been no account. Capital holds responsibility for granting him the inappropriate trading account, so its responsibility extends to the events and consequences that flowed from that.*"

What must Capital do?

In line with the redress findings in the PD (as quoted above), and for the reasons given in those findings, I order Capital to do as follows –

- Calculate the total of all Mr P's capital deposits that were lost in his trading account. ['A']

- If Mr P withdrew and retained any trading profits during the course of the account's operation, the total of all such withdrawn trading profits should be deducted from A. The aim is to ensure that he recovers only the total *capital* he invested and lost in the account, as though he never opened and operated the account, so he should not be unjustly enriched by retaining such withdrawn profits.

  It has been assumed that either Mr P had no remainder of capital in his account balance when his trading stopped or that, if he did, such remainder has already been returned to him. If any such remainder is still outstanding, it should be added to A.

A, plus any unreturned remainder capital, minus any withdrawn trading profits = ‘B’

- If only A applies to the calculation of redress for Mr P, then calculate interest on A at the rate of 8% simple per year from when each capital loss occurred (and for each specific capital loss amount) up to the date of settlement. This total interest = ‘C’.

- If B applies to the calculation of redress for Mr P, then calculate interest on B at the rate of 8% simple per year from the last date of his capital losses to the date of settlement. This total interest = ‘D’.

  This will be a fairer and simpler calculation of interest given the additions and deductions in B.

- Pay Mr P either A + C or B + D, whichever is applicable.

- In addition, pay Mr P £300 for the trouble and upset the matter has caused him.

My final decision

For the reasons given above, I uphold Mr P’s complaint and I order Capital Com (UK) Limited to calculate and pay him compensation as set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr P to accept or reject my decision before 3 April 2024.

Roy Kuku
Ombudsman