DRN-5170857

The complaint

Mrs O complains she was mis-sold a minibond investment by EGR WEALTH LIMITED (formerly EGR Broking). She says EGR failed to meet its obligations to her when selling the investment.

What happened

In April 2020, Mrs O made an application to invest £20,000 in a minibond product to be held in an ISA. She was due to receive interest at a rate of 8.1% per annum, with payments due to be paid twice a year in March and September. The investment was due to mature in December 2022.

Mrs O was introduced to the opportunity by EGR. She completed the required application paperwork it provided – this included a suitability and appropriateness test. As part of the application she signed a declaration to indicate she was a restricted investor.

In 2022, problems emerged with the investment as there were delays in payment of interest. In May 2022, EGR sent investors an update from the bond issuer, which apologised for the lack of communication regarding interest payments and explaining further issues with the performance of the investment. Then in September 2022, EGR sent Mrs O notification that the bond issuer had been placed into administration as of 1 August 2022.

In January 2023, Mrs O raised a complaint with EGR about the mis-selling of her investment. EGR responded but didn't uphold the complaint. In summary it said:

- EGR did not advise Mrs O, it only provided an "Execution Only" service, so there was no requirement to assess suitability.
- Based on the information that EGR received at the time about her circumstances, Mrs O appeared appropriate for the product. EGR carried out the necessary due diligence by providing her with the required risk disclosures and questionnaire on knowledge, understanding risks and classification certification.
- In the "Understanding Risks" section of the account opening form, Mrs O ticked "Yes" to confirm she understood it was a high-risk investment and there was no guarantee of receiving the indicated returns.

As Mrs O remained unhappy with the response, she referred the complaint to this service for an independent review.

One of our investigators issued an initial assessment upholding the complaint. In summary she said:

- There was insufficient evidence to say EGR advised, Mrs O to invest, but said it did still have obligations when arranging the investment.
- Mrs O completed a restricted investor declaration, suggesting she did meet one of the categories of investor who could be promoted this type of investment. She also indicated in her application that she had sufficient wealth to meet the high net worth (HNW) categorization. But this only covered part of the obligations on EGR when arranging investments of this type.
- EGR failed to meet its obligations with regards to ensuring the investment was

appropriate for Mrs O. The appropriateness test completed by EGR failed to adequately establish whether she was knowledgeable and experienced in this type of investment and the risks it involved. And had it met its obligations, that likely would have led EGR to the reasonable conclusion that this bond wasn't appropriate for Mrs O.
- Taking that into account, along with the information that EGR ought reasonably to have known about Mrs O and its duty to act in her best interest, it shouldn't have allowed the application to go ahead. So, the investigator recommended EGR compensates Mrs O due to its failings.

EGR didn't accept the investigator's opinion and asked for an ombudsman to reach a decision. In summary it said:

- It disputes the investigator's interpretation of its obligations under COBS 10 in relation to client knowledge and experience. It is concerned the investigator's view has been coloured by subsequent changes made by the FCA to COBS 10 and the appropriateness test, which were only introduced with effect from December 2022 / February 2023.
- EGR gathered sufficient information to be satisfied that Mrs O had the experience and knowledge to be able to understand the risks involved and whether the investment was appropriate. The risks were clearly set out and explained in the Information Memorandum ("IM"). Mrs O can have been in no doubt as to the nature of the business into which she was considering investing and the market for the relevant loan products.
- Based on the information now provided about her circumstances (that she had little or no investment experience), EGR is concerned Mrs O provided deliberately misleading information about her experience during the sales process.
- EGR gathered information that established Mrs O was a potential investor who confirmed she had relevant investment experience, was prepared to take a greater degree of investment risk in relation to an investment that would comprise less than 10% of her portfolio, and that she understood the risks involved. It doesn't accept it was required to "probe" into Mrs O's experience – the rules did not require that.
- Even if Mrs O was given a warning about the appropriateness of the investment, on balance, it would have made no difference to the outcome as the issues around the high risk illiquid and unprotected nature of the investment had already been highlighted and had no impact on her, and Mrs O would have proceeded regardless of any warning.

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.

What role did EGR play in the sale of the investment?

I've firstly considered EGR's involvement in the arrangement of Mrs O's investment. It says it provided an execution only service and it didn't make a personal recommendation or assessment of suitability. I've considered the submissions EGR make on this point. I accept there isn't evidence of regulated advice being provided by EGR.

I've looked at the evidence available to show what EGR's involvement was. I've seen details of the application process. There is evidence of an application form provided by EGR that consisted of two stages, designed to meet the rules restricting who the bond could be promoted to and on how to test whether the investments were appropriate for the potential investor. The application form Mrs O completed in April 2020 indicates she was categorised

as a ‘Restricted Investor’. There was also an appropriateness test which asked questions about her knowledge and experience.

It’s clear that EGR played an active and significant role in the arrangements of Mrs O’s investment. I am satisfied Mrs O’s complaint relates to a regulated activity. The bond was a security or contractually based investment specified in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (“RAO”). At the time Mrs O made her investment, the RAO said regulated activities include arranging deals in investments. I am satisfied the application process involved making arrangements for Mrs O to invest and had the direct effect of bringing about the transaction.

Did EGR meet its obligations to Mrs O in the arrangement of the investment?

Mrs O’s complaint concerns what she considers to be a mis-sale of the investment. I’m satisfied that this includes EGR applying relevant tests regarding investor categorisation and appropriateness. Therefore, I will first set out the relevant considerations when looking at the application process EGR conducted before allowing Mrs O to invest.

Relevant considerations

I have carefully taken account of the relevant considerations to decide what is fair and reasonable in the circumstances of this complaint. In considering what is fair and reasonable in all the circumstances of this complaint, I have taken into account relevant law and regulations; regulators rules, guidance and standards; codes of practice; and where appropriate, what I consider to have been good industry practice at the relevant time.

In my view the key consideration as to what is fair and reasonable in this case is whether EGR met its regulatory obligations when it carried out the acts the complaint is about. I consider the following regulatory obligations to be of particular relevance here.

The Principles for Businesses, which are set out in the FCA’s Handbook “are a general statement of the fundamental obligations of firms under the regulatory system” (PRIN 1.1.2G). I think Principles 6 (Customers’ interests) and 7 (Communications with clients) are relevant here.

Principle 7 overlaps with COBS 4.2.1R (1) (A firm must ensure that a communication or a financial promotion is fair, clear and not misleading), which I also consider to be relevant here.

I’m satisfied the investment Mrs O applied for was a non-readily realisable security (NRRS) and therefore there were rules restricting who this type of product could be promoted to and how to test whether the investment was appropriate for the potential investor.

These rules were set out in COBS 4.7 and COBS 10. I have set out below what I consider to be the relevant rules, in the form they existed at the time Mrs O invested.

COBS 4.7 - Direct offer financial promotions

COBS 4.7.7R said:

“(1) Unless permitted by COBS 4.7.8 R, a firm must not communicate or approve a direct offer financial promotion relating to a non-readily realisable security a P2P agreement or a P2P portfolio to or for communication to a retail client without the conditions in (2) and (3) being satisfied.

(2) The first condition is that the retail client recipient of the direct-offer financial promotion is one of the following:
(a) certified as a 'high net worth investor' in accordance with COBS 4.7.9 R;
(b) certified as a 'sophisticated investor' in accordance with COBS 4.7.9 R;
(c) self-certified as a 'sophisticated investor' in accordance with COBS 4.7.9 R; or
(d) certified as a 'restricted investor' in accordance with COBS 4.7.10 R.

(3) The second condition is that the firm itself or:
(a) the person who will arrange or deal in relation to the non-readily realisable security; or
(b) the person who will facilitate the retail client becoming a lender under a P2P agreement or a P2P portfolio,

will comply with the rules on appropriateness (see COBS 10 and COBS 10A) or equivalent requirements for any application or order that the firm or person is aware, or ought reasonably to be aware, is in response to the direct offer financial promotion."

COBS 10 – Appropriateness

At the time COBS 10.1.2 R said:

"This chapter applies to a firm which arranges or deals in relation to a non-readily realisable security, derivative or a warrant with or for a retail client, other than in the course of MiFID or equivalent third country business, or facilitates a retail client becoming a lender under a P2P agreement and the firm is aware, or ought reasonably to be aware, that the application or order is in response to a direct offer financial promotion."

COBS 10.2.1R said:

"(1) When providing a service to which this chapter applies, a firm must ask the client to provide information regarding his knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded so as to enable the firm to assess whether the service or product envisaged is appropriate for the client.
(2) When assessing appropriateness, a firm must determine whether the client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or service offered or demanded."

COBS 10.2.2R said:

"The information regarding a client's knowledge and experience in the investment field includes, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved, information on:
(1) the types of service, transaction and designated investment with which the client is familiar;
(2) the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;
(3) the level of education, profession or relevant former profession of the client"

COBS 10.2.6G said:

"Depending on the circumstances, a firm may be satisfied that the client's knowledge alone is sufficient for him to understand the risks involved in a product or service. Where reasonable, a firm may infer knowledge from experience."

COBS 10.3.1R said:

"(1) If a firm considers, on the basis of the information received to enable it to assess appropriateness, that the product or service is not appropriate to the client, the firm must warn the client."

COBS 10.3.2R said:

"(1) If the client elects not to provide the information to enable the firm to assess appropriateness, or if he provides insufficient information regarding his knowledge and experience, the firm must warn the client that such a decision will not allow the firm to determine whether the service or product envisaged is appropriate for him."

COBS 10.3.3G said:

"If a client asks a firm to go ahead with a transaction, despite being given a warning by the firm, it is for the firm to consider whether to do so having regard to the circumstances."

Having taken careful account of these relevant considerations, to decide what is fair and reasonable in the circumstances, and given careful consideration to all EGR has said, I'm satisfied the complaint should be upheld. I'll explain my findings below.

COBS 4.7 says that a firm must not communicate a direct or approve a direct offer financial promotion relating to a NRRS unless two conditions are satisfied.

The first condition is the client has been certified or has self-certified as one of the categories listed.

There is evidence that Mrs O certified as a Restricted Investor – in that she signed a declaration in this respect.

The application gave a definition of a Restricted Investor in a statement – this says:

"I make this statement so that I can receive promotional communications relating to non-readily realisable securities as a restricted investor. I declare that I qualify as a restricted investor because:

- *In the twelve months preceding the date below, I have not invested more than 10% of my net assets in non-readily realisable securities, and*

- *I undertake that in the twelve months following the date below, I will not invest more than 10% of my net assets in non-readily realisable securities.*

I accept that the investment to which the promotions will relate may expose me to significant risk of losing all of the money or other property invested. I am aware that it is open to me to seek advice from an authorised person who specialises in advising on non-readily realisable securities."

Later in the application Mrs O has indicated that she has invested £200,000 in this type or similar instruments. There is only limited information recorded about her assets at the time, so it is unclear from this whether her declaration as a restricted investor is accurate and she only had, or would only be, investing 10% of her assets in NRRSs.

But in any case, it seems Mrs O may have met one of the other criteria that would allow NRRSs to be promoted to her, as she has indicated in the application that she held assets over £250,000. This would mean she could be certified as HNW investor. Although, I haven't seen evidence to show exactly what assets she held at the time from the point-of-sale information.

Whilst not clear, it does seem possible that Mrs O did meet one of the categories under COBS 4.7.7R - that being a HNW investor. While I do have some reservations on this, it still possible the promotion could have been made to Mrs O if she indeed did meet the criteria. But even if Mrs O met the HNW criteria, this would only satisfy the first condition of COBS 4.7.7. I think EGR failed to satisfy the second condition – compliance with the rules relating to appropriateness under COBS 10.

The second condition set out in COBS 4.7.7R required EGR to comply with the rules on appropriateness, set out in COBS 10 and quoted earlier in my findings. The rules at the time (COBS 10.2.1R) required EGR to ask Mrs O to provide information regarding her knowledge and experience – and for this information to be relevant to the product offered (the first limb of the rule). The rules required that information to then be assessed, to determine whether Mrs O did have the necessary experience and knowledge in order to understand the risks involved (the second limb of the rule).

As set out above, COBS 10.2.2 R required EGR, when considering what information to ask for, to consider the nature of the service provided and the type of product (including its complexity and risks). It needed to think about asking questions on:

- the types of service, transaction and designated investment with which the client is familiar;
- the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;
- the level of education, profession or relevant former profession of the client.

Having reviewed the appropriateness test Mrs O was directed to complete during her initial application in April 2020, I'm not persuaded EGR, asked for an appropriate amount of information about her knowledge and experience, as required by COBS 10.2.1R and COBS 10.2.2 R.

The questions asked were limited and, in my view the answers given by Mrs O do not demonstrate the necessary experience and knowledge in order to understand the risks. Whilst I accept that, depending on the circumstances, a firm may be satisfied that the client's knowledge alone is sufficient for them to understand the risks involved in a product or service (COBS 10.2.6G), I'm not persuaded Mrs O had the sufficient knowledge here.

I note Mrs O positively answered a question about whether she had made a similar investment in the past, but little detail is given about what this was, and only says £200,000 invested on two occasions. This is in contrast to the application stating she hadn't invested more than 10% of her assets in NRRS. For both of these answers to be accurate, it would suggest Mrs O had a very significant level of assets. But in her submissions to this service, she doesn't recall having other investments of this type before. I haven't seen any other evidence that she held investments of the type she invested in through EGR prior to this. All of this leads me to question the information recorded. The limited questions and lack of detail provided means I don't find EGR could have made the assessment it was obliged to about appropriateness to support Mrs O did have the knowledge and experience required. I haven't seen EGR attempted to do anything further to satisfy itself of her knowledge and understanding. The relevant obligations are placed upon EGR, not Mrs O.

I note the points EGR makes about Mrs O deliberately providing misleading information. But I haven't seen anything to support this was the case. The limitations to the process and questions asked mean it isn't possible to say Mrs O failed to accurately disclosed everything she should have or made a deliberate attempt to mislead.

EGR says the sales paperwork shows that Mrs O understood the risks involved and that the investment was appropriate for her. I don't agree this is sufficient to say it fulfilled its obligations under COBS 10. While EGR doesn't think it needed to probe or gain any additional information than what is recorded when assessing appropriateness, I disagree, the assessment completed doesn't, in my view, gather sufficient evidence for it to reach a decision to assess appropriateness. This is based on the requirements at the time, and not the more recent regulatory updates EGR refer to.

Taking all of the evidence into account, I'm not persuade EGR did adequately test whether Mrs O had the knowledge to understand the risk associated with this type of complex investment. The evidence available doesn't support that she was experienced in investing in NRRSs and rather her level of knowledge was limited. The risks of the bond were complex and multifactorial. It was not, for example, a question of whether Mrs O simply understood money could be lost – but whether she was able to understand how likely that might be and what factors might lead to it happening.

As the first limb of COBS 10.2.1R was not met EGR was unable to carry out the assessment required under the second limb. EGR should have been confident, from the information it asked for, that it was able to assess if Mrs O had the necessary experience and knowledge in order to understand the risks involved with investment in the bond. But it was not in a position to make such an assessment, based on the information it obtained. I accept that taking Mrs O's appropriateness test answers in isolation would suggest she knew her capital would be at risk, But as mentioned, I've not seen that this would demonstrate an understanding of how likely it would be that she could lose her capital and/or what factors might lead to it happening.

Had EGR followed its obligations, I think the most likely conclusion it would have reached, was that Mrs O did not have the necessary experience and knowledge to understand the risks involved with the bond.

If EGR assessed that the bond was not appropriate, COBS 10.3.1R said a warning must be given and the guidance at COBS 10.3.3G said a business could consider whether, in the circumstances, to go ahead with the transaction if the client wished to proceed, despite the warning. I've explained my concerns about the testing of Mrs O's knowledge and experience, and had it adequately tested this, EGR would have come to the conclusion that the bond wasn't appropriate for her in the first place.

A clear, emphatic statement would have left Mrs O in no doubt the bond was not an appropriate investment for her. And she ought to have been privy to such a warning, had her appropriateness been tested in line with the requirements of the rules. Even if Mrs O still said she wanted to proceed after being given a warning, I still think there is more EGR needed to do if it had asked for appropriate information about Mrs O's knowledge and experience. In these circumstances, I think it would have been fair and reasonable for EGR to conclude it should not allow Mrs O to proceed. Had Mrs O been asked for appropriate information about her knowledge and experience this would have shown she may not have the capacity to fully understand the risk associated with the bond. I've seen no evidence to show Mrs O had anything other than a basic knowledge of investments. So, it would not have been fair and reasonable for EGR, to conclude it should proceed if Mrs O wanted to, despite a warning (which, as noted, was not in any event given).

In summary, I'm satisfied EGR did not act fairly and reasonably when assessing appropriateness. By assessing appropriateness in the way it did, it was not treating Mrs O fairly or acting in her best interests. If it had acted fairly and reasonably to meet the relevant regulatory obligations when assessing appropriateness, Mrs O would not have got beyond this stage.

I have noted the comments EGR make about the risk warnings contained in the IM. As the second condition set out in COBS 4.7.7R could not be met and things could not have proceeded beyond this; this means Mrs O shouldn't have received the IM at all. And so, any information within that cannot now reasonably be relied on to show she was aware of the risks associated with the bond. I've also not seen sufficient evidence to show Mrs O had the capacity to fully understand the IM – a lengthy and complex document – given this limited knowledge and experience. As such, EGR can't fairly rely on any possible reading of this as a means to correct the failings set out above.

Firstly, Mrs O should not have been able to proceed had EGR acted fairly and reasonably to meet its regulatory obligations. I acknowledge that other parties may have caused or contributed to Mrs O's losses but, notwithstanding that, I'm satisfied it is fair to ask EGR to compensate Mrs O as the appropriateness test was a critical stage, for which it was responsible for.

Secondly, for the reasons I have given, I am not in any event persuaded Mrs O did proceed with a full understanding of the risks associated with the bond. I am not persuaded she looked at the full detail of the acknowledgements she gave, given what Mrs O has said about her understanding of the bond and investment experience. I am not persuaded Mrs O had the capacity to fully understand the risks associated with the bond – and she was in this position because EGR did not act fairly and reasonably to meet its regulatory obligations at the outset. I'm therefore satisfied it is fair to ask EGR to compensate Mrs O for the losses she claims.

Putting things right

In assessing what would be fair compensation, I consider that my aim should be to put Mrs O as close to the position she would probably now be in if she had not made her investment.

I take the view that Mrs O would have invested differently. It is not possible to say *precisely* what she would have done differently. But I am satisfied that what I have set out below is fair and reasonable given Mrs O's circumstances and objectives when she invested.

What must EGR do?

To compensate Mrs O fairly, EGR must:

- Compare the performance of Mrs O's investment with that of the benchmark shown below and pay the difference between the *fair value* and the *actual value* of the investment. If the *actual value* is greater than the *fair value*, no compensation is payable.

- EGR should also add any interest set out below to the compensation payable.

- Pay to Mrs O £200 for the worry caused by the total loss of her investment.

Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Access Commercial Investors 4 Plc Bond	Still exists but illiquid	Average rate from fixed rate bonds	Date of investment	Date of my final decision	8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance)

Actual value

This means the actual amount payable from the investment at the end date.

If at the end date any asset is illiquid (meaning it could not be readily sold on the open market), it may be difficult to work out what the *actual value* is. In such a case the *actual value* should be assumed to be zero. This is provided Mrs O agrees to EGR taking ownership of the illiquid assets, if it wishes to. If it is not possible for it to take ownership, then it may request an undertaking from Mrs O that she repays to EGR any amount she may receive from the portfolio in future.

Fair value

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

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, EGR should use the monthly average rate for one-year fixed-rate bonds as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

Why is this remedy suitable?

I have decided on this method of compensation because:

- Mrs O wanted to achieve a reasonable return without risking any of her capital.

- The average rate for the fixed rate bonds would be a fair measure given Mrs O's circumstances and objectives. It does not mean that Mrs O would have invested only in a fixed rate bond. It is the sort of investment return a consumer could have obtained with little risk to their capital.

My final decision

I uphold the complaint. My decision is that EGR WEALTH LIMITED should pay the amount calculated as set out above.

EGR WEALTH LIMITED should provide details of its calculation to Mrs O in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs O to accept or reject my decision before 13 January 2025.

Daniel Little
Ombudsman