DRN-2455591

Financial Ombudsman Service

The complaint

Mr W complains that he was given unsuitable advice by M&S Financial Solutions to transfer his occupational pension (OPS) into a Self-Invested Personal Pension (SIPP) and invest his funds through a Discretionary Fund Manager (DFM).

M&S Financial Solutions was an appointed representative of Pi Financial Ltd at the time of the advice, so Pi are responsible for M&S's actions and this complaint. I'll refer to Pi throughout this decision for ease of reading.

What happened

In September 2017, Pi recommended Mr W to transfer his OPS into a SIPP and use Mayfair Capital as his DFM. Mr W followed the recommendation and opened the SIPP and a trading account with Mayfair. He transferred his pension worth around £802,000 into the SIPP and Pi's initial adviser fees of £16,000 were deducted. Mr W then took a lump sum of 25% in tax-free cash and requested a monthly gross income of £1,350 to be paid to him from his flexi-drawdown plan which was set up to be paid from November 2017.

In 2019, Mr W complained to Pi. He said he wasn't aware that the initial adviser fee would be deducted before the tax-free cash was calculated. This meant he only received £196,000 in tax-free cash, rather than the £200,000 he had expected. So he was £4,000 short. When he told Pi about this they paid him £400 back.

Mr W also thinks he was not invested in line with his balanced attitude to risk. He said he had agreed to 20% of his funds to be invested in higher risk funds, but he didn't know he was down £170,000 until he asked the SIPP and DFM for a valuation. He thinks Pi as his adviser should have told him about this.

He also is unhappy that he can't transfer his pension to another provider now as some of his funds are tied up in a bond for five years. And he believes Pi did not provide a service for their ongoing fees.

Our investigator upheld Mr W's complaint about being unsuitably advised to go into a SIPP with a DFM. She also didn't think there was sufficient evidence Pi had provided an ongoing service to Mr W.

Pi disagreed, so the complaint was passed to me for a decision.

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.

Tax free cash difference

I've seen an email dated 13 September 2017 from Mr W to Pi explaining that he wanted to take *tax free cash of 25%, i.e. £200,512 before fees are deducted* which was acknowledged by the adviser on the same day. So Pi knew what Mr W was expecting. And Pi did complete the flexible drawdown application with Mr W stating he wanted maximum tax-free cash. I'm not sure what was discussed around this, however even if Mr W was given wrong or misleading information in this regard, I agree with the investigator that Mr W hasn't financially lost out as a result. And the £400 paid by Pi in compensation is reasonable to compensate for any loss of expectation or upset Mr W experienced in relation to this.

Suitability of advice to transfer his funds into a SIPP and use a DFM

The investigator clarified with Mr W that his complaint is not about the advice to transfer out of his OPS itself, so I want to be clear that this decision does not deal with this aspect of Pi's advice.

I considered whether it was suitable advice to recommend a SIPP and DFM to Mr W.

Mr W wanted to take a large amount of tax-free cash and then draw a regular income, so I think a SIPP with a drawdown facility generally wasn't inherently unsuitable in his circumstances. The SIPP recommended had reasonable annual charges as far as I can see.

However, I'm not persuaded using a DFM arrangement was a suitable proposition for Mr W.

At the time of the advice Mr W was 63, widowed, being fully retired and living off his savings. He had an unencumbered home worth £90,000 and investment portfolio of around £48,000 made up of property bonds and emergency savings of £40,000. His pension worth over £800,000 was his only retirement provision.

A knowledge and experience questionnaire showed that Mr W's only investment experience was in relation to savings accounts, regular saving vehicles and investment bonds, all of which he took out with advice. From what I've seen I would consider Mr W to be a relatively inexperienced investor without any significant financial knowledge.

Mr W was identified to be a balanced investor. From what I've seen Mr W hasn't disputed that he was prepared to take some risk with his pension and the suitability report mentioned that he accepted he couldn't invest all his monies in a cautious manner in order in achieve returns that beat inflation. So I think investing his funds in balanced way wasn't unsuitable.

Pi's ongoing adviser fees were 0.75% per year paid annually in advance. In return for this charge, Pi said they would discuss Mr W's circumstances with him every six months and track his progress against his plan and provide an annual review of Mr W's overall financial situation. They said in their suitability report they may also recommend rebalances to Mr W's chosen funds where necessary to ensure it remained in line with his attitude to risk.

The DFM charged 1.5% dealing commission as well as additional charges which depended on how Mr W's funds would be invested. I can't see that Pi gave Mr W more details around this.

A stakeholder pension or other personal pensions were deemed less suitable for Mr W as a SIPP offered a wider range of fund choices. The DFM was recommended as Mr W would receive active management of his funds which would offer the ability to react quickly to market conditions.

However, the DFM arrangement added a layer of complexity and charges that Mr W, in my view, didn't need. He wasn't a particularly experienced investor and his main objective was to ensure his pension provided him a steady retirement income of £15,000 a year. I don't think he had the necessary experience and knowledge to understand the bespoke investment propositions a DFM would give to him and he was paying a premium charge for this.

I can't see that a wider range of funds or a bespoke investment portfolio was necessary to meet Mr W's objectives. There was no reason why he couldn't have invested in a more standard portfolio which could have been reviewed by Pi regularly during their ongoing service to make sure it was still in line with his attitude to risk and meet his requirements.

In fact the suitability report set out a balanced portfolio which was invested in global and smaller equities, government and corporate bonds as well as cash. Pi said the DFM would contact Mr W with suggestions of investments, *'typically in FTSE 100 companies'.* In my view this kind of investment allocation could have been achieved without the need to pay additional charges for a DFM which would reduce the returns on his pension unnecessarily.

Whilst Pi compared different DFMs, I can't see that simpler and cheaper investment options without a DFM were properly explored. So I don't think it was made clear that he was paying a premium for a service that wasn't a necessity.

Overall, I don't think a DFM arrangement was in Mr W's best interest and the additional costs weren't justified in his circumstances.

Pi also had a duty to ensure the recommended DFM was appropriate and do their due diligence on the firm they were recommending.

The Financial Services Authority (FSA) issued guidance in July 2012 about the recommendation of DFMs *('Assessing suitability: Replacement business and centralised investment propositions').* And the Personal Finance Society build on this in February 2015 with a good practice guide for advisers to help them develop their approach on due diligence into DFM firms.

Both regulatory and industry guidance made it clear that advisers needed to do some due diligence on a DFM before recommending their services which included for example research into their reputation and financial standing as well as the types of underlying assets the DFM would invest in and their approach to investing. The good practice guide said advisers needed to *'get under the bonnet'* of a DFM's *'marketing blurb'* and were required to question and challenge information that was provided to them. Given that the DFM was only established in 2016 and authorised a few months before Pi recommended them to Mr W, particular care should have been taken. Pi provided evidence of some due diligence questionnaire they sent to the DFM. How this was completed in August 2018, nearly a year after the advice was given to Mr W.

Based on valuations I've seen it looks like Mr W ended up in investments which were higher risk than suitable for him. And I think the risk of him ending up in this situation could have been reasonably avoided by Pi. They should have taken more care to ensure the DFM would stick to the kind of balanced portfolio and investments in mainly FTSE 100 companies as they had set out in their suitability report to Mr W. Pi didn't provide any evidence to show that any such inquiries or checks were made. I don't consider recommending the DFM and then relying on them providing suitable advice without doing any proper due diligence into the DFM and their investment strategy beforehand was sufficient.

I've seen the application to open a trading account for the DFM and their terms of business. Both refer to investments in AIM, penny shares and companies trading on the NEX Exchange.

The application form also asks clients to complete their preferred product classes and how much they would like to invest into different assets. Following the form in line with a balanced portfolio, 15% would be invested into high risk and speculative investments. These were described as Global Small Equities (e.g. AIM) & Non-Investment Grade Corporate bonds. I think such a percentage was high for a balanced investor and Pi should have queried such an asset strategy further and asked for more information about what sorts of bonds Mayfair would usually consider in here and what due diligence they would do on the investments.

Pi was also providing an ongoing service for Mr W. Mr W invested over £585,000 in October 2017 with Mayfair and a year later it was only worth around £432,000. Even taking into account that Mr W had taken annual net income of £15,000, these were significant losses that should have raised concerns whether the investments matched Mr W's attitude to risk.

Responsibility for investment losses

Pi says Mayfair was responsible for the suitability of the investments and so they are the ones who should be held to account here.

I appreciate that Mayfair is regulated and had their own responsibilities towards Mr W. And I acknowledge that they might be separately responsible for Mr W's losses. However, I'm deciding the complaint against Pi and I think they could have avoided Mr W's losses. As I explained above, I don't think Pi should have recommended Mr W to invest through a DFM at all. So with suitable advice Mr W wouldn't have ended up in the DFM and in the position he is in now. In addition, from what I've seen Pi failed to do proper due diligence on the DFM to ensure they fully understood the DFM's investment strategy and whether it was appropriate for Mr W's circumstances. If they had done so, I think they ought to have realised that the DFM's investment strategy included speculative investments which likely weren't suitable for Mr W.

So in the circumstances of this case I consider it fair and reasonable that Pi compensates Mr W for all is losses. If Pi feels Mayfair is also at fault here, they are free to pursue them directly after they have compensated Mr W in full.

I can see that Pi's adviser informed Mr W in September 2018 that M&S Financial would be closing and that he would move to another firm which also would also be an appointed representative of Pi. He said he wanted to keep Mr W as a client. However, I don't think it was made particularly clear that ongoing advice would cease and when. Mr W asked Pi for a valuation and said he would be back in touch. On 18 January 2019, the adviser contacted Mr W (from an M&S email address) to say he had liaised with Mayfair to change his risk approach to cautious and to give him information about a bond in Mr W's portfolio. He was still in my view very much involved at this point. He said if Mr W wanted ongoing advice to continue he needed to return some paperwork. Follow up correspondence indicates that Mr W told Pi he was receiving guidance from a third party. It seems Mr W made the decision not to use the services of Pi anymore.

I considered requesting Pi to calculate losses up until today. As I said above, if Pi had given suitable advice Mr W wouldn't have ended up in the DFM and riskier investments at all. So ending an adviser relationship does not necessarily mean they wouldn't be responsible for losses after this point. However, after January 2019 it looks like Mr W was relying on advice and guidance from another adviser. And so, like the investigator, I think it's fair in the circumstances that losses should be calculated until January 2019 and brought up to date with an index.

Putting things right

To compensate Mr W fairly, Pi must:

- Compare the performance of Mr W's investment with that of the benchmark shown below. If the *actual value* is greater than the *fair value*, no compensation is payable. If the *fair value* is greater than the *actual value* there is a loss and compensation is payable. Pi should add interest as set out below.

  If there is a loss, Pi should pay into Mr W's pension plan to increase its value by the amount of the compensation and any interest. The amount paid should allow for the effect of charges and any available tax relief. Compensation should not be paid into the pension plan if it would conflict with any existing protection or allowance.

  If Pi is unable to pay the compensation into Mr W's pension plan, it should pay that amount direct to him. But had it been possible to pay into the plan, it would have provided a taxable income. Therefore the compensation should be reduced to *notionally* allow for any income tax that would otherwise have been paid. This is an adjustment to ensure the compensation is a fair amount – it isn't a payment of tax to HMRC, so Mr W won't be able to reclaim any of the reduction after compensation is paid.

  The *notional* allowance should be calculated using Mr W's actual marginal rate of tax It's reasonable to assume that Mr W is a basic rate taxpayer, so the reduction would equal 20%.

- Pay Mr W £ £250 to compensate him for the worry and concern the losses to his pension have caused him when he realised he possibly lost all his retirement funds.

Investment	Status	Benchmark	From ("start date")	To ("end date")	Loss brought up to date
Mayfair portfolio in SIPP	Still exists	For half of the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds	Date of investment	31 January 2019	The calculated loss should be updated to the date my final decision by using the same index

Actual value

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

Fair value

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

Any additional sum that Mr W paid into the investment should be added to the *fair value* calculation at the point it was actually paid in.

Any withdrawal, income or other distributions paid out of the investment should be deducted from the fair value calculation at the point it was actually paid so it ceases to accrue any return in the calculation from that point on. If there is a large number of regular payments, to keep calculations simpler, I'll accept if Pi totals all those payments and deducts that figure at the end.

Why is this remedy suitable?

I've chosen this method of compensation because:

Mr W wanted capital growth and income with a small risk to his capital.

Pi must pay the compensation within 28 days of the date on which we tell them Mr W accepts my final decision. If they pay later than this they must also pay interest on the compensation from the date of my final decision to the date of payment at 8% a year simple.

Income tax may be payable on any interest paid. If Pi deducts income tax from the interest, it should tell Mr W how much has been taken off. Pi should give Mr W a tax deduction certificate in respect of interest if Mr W asks for one, so he can reclaim the tax on interest from HM Revenue & Customs if appropriate.

My final decision

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £160,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £160,000, I may recommend the business to pay the balance.

Pi should provide details of its calculation to Mr W in a clear, simple format.

Determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My decision is that Pi should pay Mr W the amount produced by that calculation – up to a maximum of £160,000 (including distress or inconvenience but excluding costs) plus any interest on the amount set out above.

Recommendation: If the amount produced by the calculation of fair compensation exceeds £160,000, I recommend that Pi pays Mr W the balance plus any interest on the amount as set out above.

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

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 21 March 2022.

Nina Walter
Ombudsman