DRN-3503554

The complaint

Mr and Mrs P complain about the investment advice given to them by Nationwide Building Society, which they say was unsuitable for them.

Mr and Mrs P are being represented by a Claims Management Company ('CMC'). All references to Mr and Mrs P include submissions made by the CMC.

What happened

The background to this complaint was set out in my provisional decision dated 9 May 2022, as follows:

Mr and Mrs P met with a Nationwide adviser (the 'adviser') in June 1997. A 'Personal Financial Review' ('PFR') was prepared by the adviser on 11 June 1997. Amongst other things, this showed Mr and Mrs P circumstances as follows:

- They were both 58 years old.
- They jointly owned a mortgage free property valued at around £55,000.
- They had savings of around £32,000.
- Their total monthly income was around £1,200 with total disposable income of £735.
- They had no debts.
- They had never invested before.
- Mr P was planning on retiring within seven years (from 1997) but neither he nor his wife had any pension plans in place.
- Their main priorities were retirement planning, savings/ investing for the future and reviewing their tax liabilities.

The adviser also prepared a 'Financial Planning Report Part 1 - Recommendations' (the 'suitability report'). In this the adviser made the following recommendations:

- From their savings Mr and Mrs P were advised to keep £7,000 each for short-term savings and for use in emergencies. They agreed they had £18,000 in total from their savings from which they wanted to invest.
- Their attitude to investment risk ('ATR') was assessed as 'balanced' meaning they were: *"…willing to accept a moderate degree of risk in order to achieve a potentially higher rate of return over a medium to longer term i.e. five years or more."*
- The adviser discussed various types of options for how to use their capital including bank or building society accounts, tax exempt special savings accounts, National Savings and general investments products.
- The adviser also highlighted the option of investing a lump sum into a pension plan. But Mr and Mrs P said they didn't want to consider this and wanted to keep their investments with Nationwide.

The adviser recommended that Mr and Mrs P invest £6,000 each in a Personal Equity Plan ('PEP') over a period of ten years. And £8,000 in a joint Guaranteed Equity Bond ('GEB') which was a six year commitment. Both were recommended because they met with Mr and Mrs P's objective for investment growth over the medium term.

The key facts document ('KFD') for the GEB described this product as a lump sum investment whose growth was linked to FTSE 100 Index. The KFD noted there was no risk to the capital but the minimum commitment was six years.

The PEP was invested in unit trust funds. There were two funds to choose from – a UK Growth Fund and a Balanced Fund. There were general risk warnings in the KFD including that the investments may not grow at the rate originally anticipated and the value of the plan wasn't guaranteed. The PEP could be cashed in at any time. And offered tax free potential growth over the medium term.

Mr and Mrs P decided to invest £5,000 each in separate PEP's. They also invested £8,000 in a joint GEB. They cashed in their respective PEP in around 2002 and received £6,078 each. They surrendered the GEB in June 2002 receiving £9,076.

In 2020 Mr and Mrs P complained to Nationwide about the sale. They said the investments didn't meet their respective attitudes to risk given they were first time investors. They also thought they were advised to invest too much over a long term particularly as the investments didn't leave them with enough available funds. Mr and Mrs P said they had to take out a loan in 1997 to buy a caravan, which they didn't think would have been needed but for the advice. They said the adviser had incorrectly assessed their outgoings needs as the assessment didn't include a car loan they had at the time.

Nationwide rejected the complaint. It considered its recommendations were suitable for first time investors. It said the GEB offered a capital guarantee and whilst the PEP wasn't guaranteed, it offered Mr and Mrs P the chance to save for their retirement in a tax-efficient way. Nationwide considered Mr and Mrs P were also provided with sufficient risk warnings about each product. Nationwide noted they (Mr and Mrs P) were mortgage free at the time, so they could afford to invest a proportion of their liquid capital over the medium term. And they were advised to put £7,000 each to one side for emergency purposes.

Our investigator didn't recommend upholding the complaint. However, I upheld this complaint in part. Mr and Mrs P accepted my provisional decision. Nationwide disagreed. In summary, it said:

- It was for Mr and Mrs P to choose the most appropriate investment from the options available to them. This was made clear in the documents at the time.
- In terms of the PEPs, the two funds available to choose from were broadly categorised as having the same level of risk.
- Our service has decided on previous occasions that up to 40% of assets held in equities of the overall portfolio is acceptable for first time investors.

So, the matter has been passed back to me for a final 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.

As set out in my provisional decision, I'm upholding this complaint in part for the following reasons:

Looking at the PFR information which I've summarised above, it's clear that Mr and Mrs P had a moderate amount to invest and they were seeking advice from Nationwide on the best way to do this. Whilst they had never invested before, this doesn't mean that the recommendation, just on this basis, was unsuitable for them. Nationwide assessed Mr and Mrs P's attitude to risk as 'balanced' and as set out above this meant they were willing to accept a moderate degree of risk in order to achieve investment growth in the medium term.

Based on Mr and Mrs P's attitude to risk and their circumstances at the time, I think the GEB was a suitable recommendation to make. It provided a guaranteed return of capital with returns in line with the FTSE 100 index. As first-time investors, I think this allowed them to meet their stated priorities with very little risk to their capital. And I think everything pointed to them being prepared to accept this level of risk.

I note what Mr and Mrs P say about the GEB in that they weren't able to withdraw money without penalties within the first six years. But from what I can see they seemed to have cashed it in after five years and didn't seem to suffer a loss as a result. I also think they were looking to invest for the medium term and they were left with sufficient savings and income to meet their assessed needs at the time.

I've also noted what Mr and Mrs P say about the car loan repayments which they said weren't included in the assessment of their outgoings. But as our investigator said, it doesn't appear the adviser was made aware of the repayments. So, I wouldn't expect this outgoing to be taken into account in the recommendations.

In terms of the recommended PEP's, I don't think these investments were suitable for Mr and Mrs P. This recommendation appears, at least in part, to have been because they were looking for a tax efficient way to save for their respective retirements. Mr and Mrs P chose to invest slightly less than that recommended with £5,000 in each PEP rather than the maximum that could be invested at £6,000. The way the PEP worked was described in the KFD as follows: *"Your payments buy units in your chosen fund(s) which aim to grow over time. As the value of the investments within the funds rises and falls, so does the value of your units."*

The KFD said there were two funds to choose from. The first was listed as a 'Balanced Fund' and was described as follows: *"The Balanced Fund aims to provide long-term growth of both capital and income by investing in a broad range of UK and overseas companies' shares and in fixed interest securities."* The second fund was a 'UK Growth Fund' and its aims were described as follows: *"…for long-term capital growth by investing in a broad range of UK companies."*

There were general risk warnings about the PEP both in the KFD and in the terms and conditions. The latter said the following: *"The value of investments and the income from them may go down as well as up and are not guaranteed. The PEP Holder may not get back the amount originally invested."* So, unlike the GEB, the PEPs didn't come with any guarantee about the return of the capital.

The 'UK Growth Fund' Mr and Mrs P were recommended to invest in, appears to have been a fund that invested almost entirely in UK equities. In my view, this appears to me to be a higher level of risk than the 'moderate' risk Mr and Mrs P were prepared to take. It was their first time investing, and as I've said, unlike the GEB, the PEP came with no guarantees about what they would receive over the medium to long term.

I take on board what Nationwide have said about Mr and Mrs P being able to commit their liquid capital due to being mortgage free and having sufficient income to meet their needs. But the amount Mr and Mrs P agreed to invest in the PEPs was almost 32% of their total savings and was recommended to meet their retirement needs. I don't think Mr and Mrs P could afford to take the type of risks that were involved in investing a significant amount of their savings in a product invested almost entirely in UK Equities. And which came with no guarantees about whether they would receive their capital back.

I've noted Nationwide's further comments to my provisional decision. However, its further submissions haven't changed my mind for the following reasons:

- Nationwide said that the risk profile between the two types of PEP investments were the same. But looking at each of the two available funds, it would appear to me that one contained proportionally more riskier assets than the other. I don't think neither Mr P nor Mrs P, as first time investors, looking to save towards their retirement, would have understood the risks associated with an investment fully reliant on equities for its growth.

- I note Nationwide's point about the client being responsible for choosing the investment. But they were being advised by a Nationwide adviser. They were dependent on that advice to make an informed choice. This was particularly the case, as the adviser noted, because they had no experience with investing previously. So, I think they needed to be properly advised, and for the reasons I've set out above, I don't think they were.

- Nationwide refer to other decisions made by our service. But as it will understand, all of our decisions are decided on an individual basis with reference to the facts of the particular case. And in this case, I don't think it properly advised Mr and Mrs P because it recommended an investment that both in terms of risk and understanding of that risk, was not suitable for them. I don't consider they would've invested so much of their available savings, which were fairly modest, in the funds if they had fully understood the risks involved.

For all these reasons, I uphold the part of Mr and Mrs P's complaint that relates to their respective PEPs.

Fair compensation

In assessing what would be fair compensation, I consider my aim should be to put Mr and Mrs P as close to the position they would probably now be in if they had not been given unsuitable advice. I think Mr and Mrs P would have invested differently. It is not possible to say *precisely* what they would have done, but I am satisfied that what I have set out below is fair and reasonable given Mr and Mrs P's circumstances and objectives when they invested in their respective PEP's.

What should Nationwide Building Society do?

To compensate Mr and Mrs P fairly, Nationwide Building Society must:

- Compare the performance of Mr and Mrs P's investments 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.

- Nationwide Building Society should also pay interest as set out below. Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
PEP (Mr P)	No longer in force	For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds	Date of investment	Date ceased to be held	8% simple per year on any loss from the end date to the date of settlement
PEP (Mrs P)	No longer in force	For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds	Date of investment	Date ceased to be held	8% simple per year on any loss from the end date to the date of settlement

Actual value

This means the actual amount paid 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.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, Nationwide Building Society 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 chosen this method of compensation because:

- Mr and Mrs P wanted capital growth with a small risk to their capital.
- The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to their capital.
- The FTSE UK Private Investors Income total return index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds. It would be a fair measure for someone who was prepared to take some risk to get a higher return.
- I consider Mr and Mrs P's risk profile was in between, in the sense that they each were prepared to take a small level of risk to attain their respective investment

objectives. So, the 50/50 combination would reasonably put Mr and Mrs P into that position. It does not mean Mr and Mrs P would've invested 50% of their money in fixed rate bonds and 50% in some kind of index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of returns Mr and Mrs P could've obtained from investments suited to their objectives and risk attitudes.

My final decision

I uphold the complaint in part. My final decision is that Nationwide Building Society should pay Mr and Mrs P the amount calculated as set out above.

Nationwide Building Society should provide details of its calculation to Mr P in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr and Mrs P to accept or reject my decision before 5 July 2022.

Yolande Mcleod
Ombudsman