DRN-3537797

The complaint

Mr and Mrs B, as trustees of the B Trust, complain that David Jameson Limited (DJL) gave them unsuitable advice to invest using a Discounted Gift Trust (DGT).

What happened

The background to this complaint is well known to both parties so I won't repeat it in detail here. In summary, Mr and Mrs B received advice from 2013 onwards to invest in a DGT with the purpose of mitigating a potential Inheritance Tax (IHT) liability.

More recently, Mr and Mrs B changed advisers and found out there was a mandatory income they needed to take from the trust fund. As this hadn't been taken before they had to withdraw a lump sum of £100,000 which triggered additional tax charges and had to be absorbed into their estate. They complained as the purpose of the advice was to reduce their estate for IHT purposes.

Our Investigator upheld the complaint as she felt the advice was unsuitable as it didn't meet Mr and Mrs B's needs of mitigating their IHT liability. She recommended DJL do the following:

- Put in place an indemnity to cover any potential IHT liability on the £100,000 lump sum and cover the cost of doing so
- Put in place an indemnity to cover any potential IHT liability on excess income, if it can be shown that income can't be stopped or reduced
- Pay for reasonable costs in assessing the tax liability on the £100,000 lump sum withdrawal, if required
- If a tax liability has been incurred, DJL should pay this; if it's already been paid then DJL needs to refund this to Mr and Mrs B adding 8% simple interest from the date of payment to HMRC to the date of settlement
- Pay for reasonable costs incurred in determining if income can be stopped or reduced, and the cost of making those changes
- Refund the adviser fees, with simple interest of 8% from the date each fee was taken to the date of settlement
- Pay Mr and Mrs B £750 for the distress and inconvenience.

Neither Mr and Mrs B nor DJL accepted the Investigator's view. DJL maintains the advice was suitable. It also made the point that it had told the bond provider where to pay the income, and what income needed to be taken so it had no responsibility for the lump sum of £100,000 having to be taken. DJL believes this has happened due to Mr and Mrs B's new adviser.

Mr and Mrs B feel they should've been advised to invest the full sum into a Business Property Relief (BPR) scheme – and would like to be put into a comparative position if that had been the case. They said that the income has fallen into their estate and they hadn't consented to a DGT being put in place.

As neither party agreed, the complaint has been 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.

Both parties have submitted very detailed information on this complaint, and I'd like to assure them that I've considered it all. However, our Investigator has covered in detail already what happened and their reasons for upholding the complaint. So, I've focused this decision on the main points of the complaint which are:

- Was the advice DJL gave to Mr and Mrs B to invest using a DGT suitable?
- If it wasn't suitable, what needs to be done to put it right.

Mr and Mrs B's circumstances and objectives

Mr and Mrs B received advice between 2013 and 2015 about the DGT. DJL has submitted the adviser notes covering this period which record some details about Mr and Mrs B. It's seems from this that they had assets totalling over £2m, surplus income every month and they were looking to mitigate IHT. It appears that they were raising funds through an equity release mortgage with the purpose of investing it in tax efficient ways to mitigate IHT. The equity release mortgage isn't the subject of this complaint so I don't intend to comment on it further. Although I will say that it doesn't appear from the adviser notes that DJL took the lending into account when determining Mr and Mrs B's assets.

Overall, it's clear that there was a potential IHT liability that Mr and Mrs B wanted to address so it's right that DJL looked into ways to mitigate this for them.

The advice

DJL advised Mr and Mrs B to invest £400,000 into a bond to be held in a DGT. I can see that DJL gave Mr and Mrs B a print-out of what a DGT was, which appears to be from an internet search, as well as information from the platform provider about how the DGT works.

DJL didn't provide Mr and Mrs B with a suitability letter setting out why it recommended the DGT. It said the adviser preferred to use notes, but by not issuing the letter, DJL hasn't complied with its regulatory duties. I've looked at the notes to understand why a DGT was recommended. Throughout the notes the adviser refers to the DGT as being tax efficient. It said the income from the bond, which isn't needed, would be used to invest in other tax efficient strategies. Although these aren't actually expanded upon.

A DGT is ordinarily set up to allow the settlors to take an income from the lump sum investment. When applying for a DGT some underwriting takes place to determine what income may be needed for life for the settlors and this portion of the investment often represents the discount – essentially that amount falls immediately outside of the estate for IHT purposes and the remainder is a Potentially Exempt Transfer – falling outside the estate after seven years. A DGT is designed to reduce IHT immediately through the settlors taking an income and can be a useful tool for IHT planning – specifically when that income is used. If the income isn't spent, it falls back into the estate which dilutes the effectiveness of a DGT for IHT planning.

DJL, as well as the platform provider, has provided us with copies of the forms used to set up the DGT. The first form didn't specify what income was to be taken, there's another form that says 5% income is to be taken over monthly withdrawals but didn't specify where to pay it. A further form DJL provided showed it asked the provider to pay the income to Mr and Mrs B's General Investment Account but this form doesn't show how frequent the withdrawals should be and how much. I've also seen notes suggesting a 3% annual income would be taken quarterly. The evidence shows that it wasn't clear how much income should be taken and where it should be paid. And I can't see Mr and Mrs B were told how to take the income, or that it was crucial to do so. On the contrary, DJL said, in its correspondence to Mr and Mrs B:

"'We are not taking any income from that source at present and nor do we need to. This is efficient from an Inheritance Tax point of view, although still has some time to run before it's fully effective"

I've also noted that there's no clear record of what discount Mr and Mrs B were to receive from the DGT. The adviser notes at some point that there's a discount of around 50% but there's nothing documented about the actual discount that applied to Mr and Mrs B when they invested.

In summary, and in the absence of a suitability letter, the advice DJL gave Mr and Mrs B was to invest £400,000 into a DGT to mitigate IHT but they also told Mr and Mrs B that they didn't need to take any income from it.

Was the advice suitable?

I can see that the Investigator concluded Mr and Mrs B's risk profile and the risk exposure of the underlying investments were likely suitable, and I'd agree based on what Mr and Mrs B have said about other investments they made and would've preferred to make in the circumstances. Following the Investigator's view there hasn't been any dispute over the risk associated with the underlying investment so I will focus on the use of a DGT.

As mentioned above, a DGT can be an effective IHT planning tool where income withdrawal is part of the objective. But Mr and Mrs B didn't need any additional income. It is recorded multiple times that they had no use for additional income and so I don't think recommending the use of a DGT was suitable. I also note that DJL told Mr and Mrs B they didn't need to take an income – which isn't correct. As 5% withdrawals were set up as part of the trust provisions, the income had to be taken. And to not take an income, or set one up, would mean this wasn't a DGT but rather a standard discretionary trust.

DJL has clarified that the income was meant to be paid to Mr and Mrs B's investment account on the same platform, and it was to be used for further tax planning. DJL has sent in forms to show that it told the platform where to pay the income. But the form it refers to doesn't outline how much income is to be taken. And the form when setting up the trust specifies 5% annually to be taken but not where to pay it. It was DJL's responsibility to ensure the forms were completed and submitted correctly and that wasn't the case here. And in any event, even if the income had been paid to Mr and Mrs B's investment account, I can't see what "further tax planning" was discussed or put in place. This may be a result of the adviser choosing to rely only on notes and not issuing a suitability letter despite being obliged to do so.

To summarise, Mr and Mrs B were advised to use a DGT when they had no need for an income. As this means that the income, that is surplus to requirements, would fall directly back into Mr and Mrs B's estate, I can't agree that it was suitable for IHT planning. It didn't meet their objectives of mitigating IHT liability as only the amount that wasn't withdrawn would fall outside of the estate and only after seven years.

Consequences of the advice

The advice DJL gave was unsuitable, and as a result Mr and Mrs B may be liable for more IHT than they would be had suitable advice been given. But crucially in this case, the fact income wasn't taken when it should've been has meant Mr and Mrs B had to take a lump sum of £100,000 which represented five years of income that they hadn't withdrawn.

DJL has said that the £100,000 withdrawal was due to new advice Mr and Mrs B received, and it isn't responsible for this. But I disagree. DJL didn't give suitable advice, didn't tell Mr and Mrs B that the income had to be taken and didn't give correct instructions about the withdrawal. The income of 5% of the investment annually must be taken as part of the trust that was set up. As it wasn't taken, in 2019 upon discovery, Mr and Mrs B had to take it as a lump sum – all of this is a direct consequence of DJL's advice.

This £100,000 appears to have fallen into Mr and Mrs B's estate – although I understand they have new advisers who are looking into ensuring it is tax efficient. Mr and Mrs B also say they incurred an income tax liability due to a chargeable gain. Overall I think it's likely that Mr and Mrs B may face some negative tax consequences as a result of DJL's unsuitable advice and DJL should provide an indemnity for these consequences.

It's also important to note here the impact this advice has had on Mr and Mrs B. The notes suggest that Mr and Mrs B put a great deal of trust into DJL and provided them with very sensitive details. Aside from the continual use of unprofessional language that I've seen in the notes, DJL didn't provide Mr and Mrs B with suitable advice. And, to find out they had to then take £100,000 as a lump sum back into their estate would've caused them significant trouble and upset. I say this specifically because they were told they didn't need to take an income, that their investment was effective for IHT planning and they were both at an age where they needed to ensure their IHT planning arrangements were in place. I agree with our Investigator that £750 compensation is fair and reasonable. And I also agree that adviser fees should be refunded. The fundamental advice wasn't suitable, the instructions provided weren't correct or clear and Mr and Mrs B weren't told how the DGT worked, that they needed to take an income or what the discount was, if there was one.

I do note that Mr and Mrs B have continually said they didn't consent to the DGT being put in place. Having considered the evidence, I don't agree that was the case. I can see Mr and Mrs B signed the relevant documents and they were told about the DGT on a number of occasions. But, as I've already explained, the advice DJL gave was unsuitable.

Putting things right

I note that Mr and Mrs B would like to be put in the position they'd have been in if they'd invested the full amount utilising BPR. I appreciate with hindsight they feel this is what they'd have done but I'm mindful that use of BPR comes with higher risks and I don't think this is the right comparison to make here. I think it's likely Mr and Mrs B are using the benefit of hindsight to decide what they feel they'd have done.

My role is to put Mr and Mrs B in the position they'd have been in had they not been given unsuitable advice – and in this case that is to ensure they don't have a higher tax liability as a consequence of DJL's errors. I'm pleased to see that the amount in the trust has been held there for seven years and falls outside of the estate now. DJL say that Mr and Mrs B haven't lost out because of this and the investment did what it was supposed to do, but I think it's fortunate that the investment has now been in place that long. I note Mr and Mrs B's new advisers are considering the options with the continual withdrawals that need to be taken and weighing up the right options for mitigating IHT going forward. This does mean it's not possible to know exactly the effects of the advice on Mr and Mrs B's estate, so to put things right we need to look to the future somewhat. With this in mind, I agree with our Investigator that DJL needs to provide Mr and Mrs B with indemnities to ensure that they haven't lost out as a result.

For clarity, I uphold this complaint and direct David Jameson Limited to put the following in place:

- Put in place an indemnity to cover any potential IHT liability on the £100,000 lump sum and cover the cost of doing so
- Pay for reasonable costs in assessing the tax liability on the £100,000 lump sum withdrawal, if required
- If a tax liability has been incurred, DJL should pay this; if it's already been paid then DJL needs to refund this to Mr and Mrs B adding 8% simple interest* from the date of payment to HMRC to the date of settlement
- Pay for reasonable costs incurred in determining if income can be stopped or reduced, and the cost of making those changes
- Put in place an indemnity to cover any potential IHT liability on excess income to be taken from the investment, if it can be shown that income can't be stopped or reduced
- Refund the adviser fees, with simple interest of 8%* from the date each fee was taken to the date of settlement
- Pay Mr and Mrs B £750 for the distress and inconvenience.

It should be noted that when I say above reasonable costs, these need to be evidenced and broken down.

*If David Jameson Limited considers that it's required by HMRC to deduct income tax from that interest, it should tell Mr and Mrs B how much it's taken off. It should also give Mr and Mrs B a tax deduction certificate if they ask for one, so they can reclaim the tax from HMRC if appropriate.

My final decision

For the reasons I've explained, I uphold this complaint. David Jameson Limited must follow the directions I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs B and Mr B to accept or reject my decision before 20 October 2022.

Charlotte Wilson
Ombudsman