DRN-3625542

The complaint

The executors for Mr M's estate complain about advice he received from Investec Wealth & Investment Limited when he set up an offshore investment bond. The bond was gifted to a trust after being set up. Mr M's executors are also the trustees for that trust.

What happened

The advice here was summed up in a letter Investec wrote to Mr M in 2007. Mr M wanted to reduce the inheritance tax his estate would have to pay when he died. Investec recommended a bond held in a discounted gift trust. Mr M set that up in 2008.

The discounted gift trust was set to return 5% of the amount Mr M had invested to him each year. But after Mr M died in 2019, the executors for his estate were surprised that these withdrawals counted towards the value of the investment for tax calculations.

Rather than the investment producing about a £40,000 gain in value over the years, it'll be seen to have gained closer to £140,000.

In response to the executors' complaint, Investec felt their advice to Mr M had been clear about what the investment was and how it would work. But they noted that in 2012 they'd told Mr M that their commission would be treated as a fee for providing him ongoing advice. Investec saw they hadn't given Mr M this advice, so they offered to refund the fee. They also offered Mr M's executors £250 for any trouble and upset caused.

Mr M's executors didn't accept that resolved their complaint, so they brought it to us. They also raised some general issues about the documents and correspondence from 2006 to 2008, that they felt showed things weren't as they should be.

Our investigator looked at the documents from the time, and considered what Investec had done to assess and meet Mr M's objectives. She felt Investec had met Mr M's objectives at the time in a reasonable way. And she felt enough had been done to explain how tax might apply to the investment in the future. But she agreed with Investec that they shouldn't have taken an advice fee without providing advice to Mr M. She said the refund for that should include a payment to represent the return that the fee would have achieved, if it had remained invested.

The executors for Mr M's estate didn't agree with that view, so the case has come to me for a formal 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.

Having done so, I find that the remedy Investec agreed with our investigator will be enough to put things right. I'll briefly explain my reasoning.

At its heart, this is a complaint about how income tax applies to the money Mr M invested now the trustees plan to encash it.

Investec's letter to Mr M in August 2007 did explain what would happen:

> *"When the investment is encashed there will be a potential tax liability, based on any gain at the rate payable by the trust, currently 40%. However, if the trustees assign the bond to default beneficiaries, any gain would fall on the beneficiaries and any gain would therefore be charged at their marginal rate of tax - which permits a degree of flexibility to manage any potential tax liability."*

What isn't covered in detail is how the gain would be calculated. Mr M's investment here began with £175,000. Its value – if encashed at the time of the complaint – would have been around £220,000. And over the years prior to that Mr M had received about £95,000.

In simple terms, the investment's gain is calculated as what came out – £220,000 if encashed, plus the £95,000 Mr M had received – minus what went in – £175,000. That comes to the roughly £140,000 mentioned in the complaint – £315,000 minus £175,000.

It's worth noting that it's not the original invested amount that's taxed – it's the gain. That tax isn't created as a result of the payments made to Mr M. If he'd received nothing from the trust instead, it'd still have as much tax to pay. It'd just have £95,000 more to pay it with.

That's ultimately where I disagree with the complaint Mr M's executors – also the trustees now holding the investment – raised. In an email to Investec following the complaint response, they wrote:

> *"The 'sales' emphasis was totally on dealing with IHT and still having some income which when one is 84 years old has an appeal. It was not explained that the income taken would create a capital gains liability in the Bond.*
>
> *"Finding a solution to one thing and creating a problem for a later date, without setting out mitigation details, is highly unsatisfactory."*

Taking the *"income"* didn't create the tax liability. So I can understand why Investec didn't warn Mr M that it would.

I can appreciate the trustees were unsighted on how income tax would apply to the investment. But I don't see that as an issue for Investec to answer when considering their advice to Mr M to set up the investment. It has some interesting features that meant income tax wouldn't be payable in Mr M's lifetime, unless he lived more than 20 years.

The payment each year to Mr M was set to 5% of the value initially invested. That's the cut-off point before income tax is payable under the tax rules that apply. And the bond couldn't otherwise be encashed while Mr M was alive.

Following Mr M's death the bond didn't automatically end – an event that would usually trigger an income tax liability. It won't end until the year 2107, unless the trustees decide to encash it before then.

The discretionary trust used also means it will be up to the trustees – not the beneficiaries – when to end the investment. And it looks like the trustees could choose to assign the investment directly to eligible beneficiaries, which would change who is responsible for paying the income tax owed, and what rate they have to pay.

The income tax to pay will – as a result – depend on how exactly the trustees choose to handle the investment. It might even be possible to pay no income tax – if they can assign the investment to a beneficiary at a point when they're either exempt from or below the threshold for paying UK income tax.

Given the unknowns at play, I'm not surprised Investec simply said there would be *"a degree of flexibility"* when it came to the income tax. They didn't need to go over every possible way income tax could end up applying to the investment Mr M was setting up for the service to be reasonable. Not when Mr M's main objective was to reduce inheritance tax.

That was achieved by having the investment in a trust. It's true that if the payments then made back to Mr M didn't match up with what he planned to use or gift during his lifetime, the effectiveness of that trust could be undermined. But I can't see Mr M's executors have made a complaint on those terms.

With regard to the complaints about items of correspondence in 2006 to 2008, I put a lot of weight in the fact Mr M didn't complain about these at the time. If he was happy with them then, I feel his executors can't legitimately complain about them now.

Similarly, the level of income Mr M was receiving seems to have been accepted by Mr M at the time. If the income level had been too high for him, he could have complained about that earlier. The fact he didn't complain speaks to his being satisfied with the income level put forward by Investec.

The only other substantial issues are then the matters Investec already offered a remedy for.

In responding to the complaint, Investec noticed they hadn't provided the advisory service they told Mr M they were charging a fee for from 2012. I agree that it makes sense to return the fee in that case. And I can see the logic in our investigator's view that the refund should be worked back in to the investment as if it hadn't been taken, so that the gains it would have achieved are included in the payment to the trust.

And I can see the trustees have commented on how long it took to get an explanation from Investec, when they started asking about the investment's gains. I find the £250 compensation payment Investec offered for the trouble and upset caused for the trustees is suitable to acknowledge that impact. I don't direct more than that, as the underlying effort needed to work out the gain and pay income tax doesn't come from any failing by Investec.

My final decision

I'm upholding this complaint on the points where Investec Wealth & Investment Limited have already identified their service wasn't reasonable. To put those issues right, Investec should:

- repay the advice fee charged from 2012 to 2014 to the investment fund.
- compensate the trust for the lost gain that money would have made if it had stayed invested.
- pay Mr M's executors – as trustees of the trust he set up – £250 to acknowledge the trouble and upset caused by the communication delays in this case.

On all other points of the complaint, I find the service has been fair and reasonable.

Under the rules of the Financial Ombudsman Service, I’m required to ask the estate of Mr M to accept or reject my decision before 21 November 2022.

Paul Mellor
Ombudsman