DRN-3728630

The complaint

Mr W says Wealthmasters gave him unsuitable advice in 2015 to invest in two high risk investments through his Self-invested Personal Pension (SIPP), namely Dolphin Trust (Dolphin) and Greyfriars Portfolio Six (P6). He also complains about a recommendation in 2017 to make a cash investment into Dolphin.

Mr W is represented by TWL Solicitors (TWL).

What happened

Mr W and Mrs W sought advice from Wealthmasters. Mr W was approaching retirement, they were also looking to review their existing Individual Savings Accounts (ISAs) and consider using monies held on account for a lump sum investment.

Information about Mr and Mrs W's objectives, circumstances and attitude to risk started to be gathered from December 2014. For example, it's recorded that:

- They had no financial dependents. Mr W was employed as a director and Mrs W worked part-time as a teacher. Their gross annual income was around £103,000. They had a net monthly disposable income of around £2,100.
- They owned their own home which was valued at £750,000. Mrs W had a rental property valued at around £120,000 which was also unencumbered. They had account deposits of around £68,000 and around £37,000 in stocks and shares ISAs.
- Mr W had personal pensions with Abbey Life (AL) and Old Mutual Wealth (OMW). At the time these were said to have transfer values of about £134,000 and £58,000 respectively. He was also a member of a group personal pension with Standard Life (SL), which his employer contributed to. This was said to be worth around £30,000. Mrs W was a member of an occupation pension scheme (OPS).
- Their general financial objectives were similar. Both prioritized maintaining their standard of living in retirement, investment planning, long-term savings and mitigating inheritance tax liabilities.
- Neither were regarded by Wealthmasters as high net worth individuals or self-certified sophisticated investors.

Mr and Mrs W were assessed by Wealthmasters as having a moderate attitude to risk. It summarised this as meaning:

"The Moderate Investor is somewhat concerned with short-term losses and may shift to a more stable option in the event of significant losses. The safeties of investment and return are typically of equal importance to the Moderate investor."

For Mr W this was translated into an investment strategy he was said to have agreed where 20% of his funds would be invested at below average risk; 60% at average risk and 20% at above average risk. No funds would be earmarked for 'adventurous' investments.

Wealthmasters produced three separate suitability reports over a relatively short period. The first and second in February and March 2015 were focussed on Mr W's pension arrangements, their ISA provider and how to utilise available cash deposits. The second report was issued because of significant changes to their circumstances. These were recorded in the following terms:

"You have sold your house and have an offer being considered on another which you intend to live in whilst you improve its current state with the view to selling the house in approximately four years for a projected profit. This will initially increase your funds held on deposit as your current property is valued at £750,000 whereas the proposed purchase is less. Having said that, you have confirmed the new house will require considerable improvements."

"However, [Mr W aims] to do much of the home improvements [himself] as [he] handed in [his] notice with [his] current employer on Friday (6'' March 2015) and intend to become self-employed with a view to working no more than two days a week. As a result your earnings are due to decrease meaning you may need to draw on your pension income sooner than you had anticipated. Also, your employer will no longer contribute into your Standard Life pension meaning you now wish to have a review of this plan as it was initially discounted in the original report whilst your employer was paying in."*

Mr W also informed Wealthmasters that rather than retiring at 60 as he'd initially intended, he now expected to continue to work self-employed but on reduced hours until he was 67, at which point he would be solely dependent on his pension arrangements.

Wealthmasters third suitability report was issued in May 2015. This was focussed on how Mr W should invest his pension funds.

As these three suitability reports are essentially connected I've considered them together. The main recommendations Wealthmasters made were that:

- Mr W should switch his AL, OMW and SL pensions to a Greyfriars SIPP in order to consolidate administration and to provide more investment possibilities both pre and post retirement. And to enable his phased approach to retirement.
- Mr W pension fund should invest: £100,000 in a portfolio managed by a Brewin Dolphin Discretionary Fund Manager (DFM), following a moderate risk strategy; £100,000 in a portfolio managed by a Sanlam DFM, following a moderate risk strategy; £36,000 in P6; £36,000 in a Structured Capital at Risk Product (SCARP) with a maximum term of six years; £36,000 in a 5-year Dolphin loan note, providing fixed income of 12%pa; and £2,000 left in cash to pay SIPP fees.
- As this would be Mr W's last year as an employed person, he should make a substantial pension contribution for the tax-year to maximise the tax-relief this would attract. Also, that Mr and Mrs W should change the provider for their ISAs and maximise their contributions for the tax-year. It noted the effect of these recommendations was utilize the bulk of their available cash deposits.

Ultimately Mr W accepted Wealthmasters' recommendations. His new SIPP was opened on 27 March 2015 with a net personal contribution of £32,000. In April 2015 about £90,500 was switched from OMW and around £144,500 from AL. In May 2015 his SIPP account was credited with £8,000 tax relief for his pension contribution. In June 2015 about £44,500 was received from his former SL pension.

Wealthmasters took its initial advice fees amounting to about £6230 in May and June 2015. And by August 2015 the bulk of his available funds had been invested in accordance with the recommendations set out.

Wealthmasters issued a further suitability report on 29 June 2017. It recommended Mr W withdraw the proceeds of a Novia ISA valued at about £18,500 and invest directly in a 5-year Dolphin loan note for £20,000. Its reasoning was Mr W required additional income to maintain his standard of living in retirement and preferred fixed income so he could predict his income from year to year. It said the Novia ISA didn't include alternative investment strategies that would provide a steady quantifiable income stream. It also noted Mr W had been very happy with his previous Dolphin investment.

On 21 October 2020, TLW raised several concerns with Wealthmasters about its advice to Mr W to invest in the Greyfriars P6 and Dolphin holdings. It wasn't satisfied that it had adhered to the appropriate regulations in providing him with advice. And it considered these recommendations had been unsuitable.

On 29 January 2021 Wealthmasters provided Mr W's representative with its final response. It refuted his complaint and summarised its position saying:

"We stand by the advice given to Mr W as suitable at that time and the documentation provided to you proves that the advice was suitable in line with regulation and his own objectives and requirements. Wealthmasters followed the correct processes, we provided Mr W with all the relevant information via face to face discussions, detailed written recommendation reports and product explanations (and the appropriate risk warnings). For these reasons Wealthmasters do not uphold Mr W's complaint."

The Investigator reviewed Mr W's complaint and upheld it. He considered that the Dolphin and P6 investments had been unsuitable for someone with a moderate risk appetite and the strategic spread of risk he'd agreed. Wealthmasters didn't respond to the Investigator's findings.

Mr W's complaint has been passed to me to review the case afresh and to issue a decision. This is the final part of our process.

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.

Where there's conflicting information about what happened and gaps in what we know, my role is to weigh the evidence we do have and to decide, on the balance of probabilities, what's most likely to have happened.

I've not provided a detailed response to all the points raised in this case. That's deliberate; ours is an informal service for resolving disputes between financial businesses and their customers. While I've taken into account all submissions, I've concentrated my findings on what I think is relevant and at the heart of this complaint.
I'm upholding Mr W's complaint. I'll explain why.

How does the regulatory framework inform the consideration of Mr W's case?

The first thing I've considered is the extensive regulation around transactions like those performed by Wealthmasters for Mr W. The FCA Handbook contains eleven Principles for businesses, which it says are fundamental obligations firms must adhere to (PRIN 1.1.2 G in the FCA Handbook). These include:

- Principle 2, which requires a firm to conduct its business with due skill, care and diligence.

- Principle 3, which requires a firm to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
- Principle 6 - which requires a firm to pay due regard to the interests of its customers.
- Principle 7 - which requires a firm to pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

So, the Principles are relevant and form part of the regulatory framework that existed at the relevant time. They must always be complied with by regulated firms like Wealthmasters. As such, I need to have regard to them in deciding Mr W's complaint.

Further, COBS 2.1.1 R requires a firm to act honestly, fairly and professionally in accordance with the best interests of its clients, in relation to designated investment business carried on for a retail client. The definition of "designated investment business" includes "arranging (bringing about) deals in investments".

COBS 9.2.1R sets out the obligations on firms in assessing the suitability of investments. They are the same things that I look at when reaching a decision about whether the advice was suitable. In summary, the business must obtain the necessary information regarding: the consumer's knowledge and experience in the investment field relevant to the advice; their financial situation; and their investment objectives.

In 2009 the Financial Conduct Authority (FCA), then the Financial Services Authority, published a checklist for pension switching that I think is still helpful today. It highlighted four key issues it thought should be focussed on:

- *Charges* - has the consumer been switched to a pension that is more expensive than their existing one(s) or a stakeholder pension, without good reason?
- *Existing benefits* - has the consumer lost benefits in the switch without good reason? This could include the loss of ongoing contributions from an employer, a guaranteed annuity rate or the right to take benefits early.
- *Risk* - has the consumer switched into a pension that doesn't match their recorded attitude to risk (ATR) and personal circumstances?
- *Ongoing fund management* - has the consumer switched into a pension with a need for ongoing investment reviews but this was not explained, offered or put in place.

Further, when considering the use of a discretionary fund management (DFM) arrangement, the regulator has made clear that amongst other matters, firms need to take into account issues such as:

- Likely cost: do the overall costs justify the potential for improved performance?
- Size of funds under management: once a consumer has a moderately-sized fund, they may benefit from a model portfolio which is rebalanced automatically by a DFM ranging all the way up to bespoke arrangements for clients with larger funds.
- Investor's knowledge and experience: FCA has said the adviser needed a reasonable belief that the investor could understand the nature of the risks of the underlying investments the DFM might make.
- Level of disclosure: whether the benefits vs cost of the arrangement were actually explained to the investor in terms they were likely to (or appeared to) understand.

The regulator was clear there was a positive obligation on the adviser to carry out this research, rather than supplying the DFM with a risk rating and hoping 'all will be right in the end'. They were recommending DFM as a solution to their client's needs and that meant 'looking under the bonnet'.

Did Wealthmasters meet the regulatory obligations it was bound by when advising Mr W?

I don't think Wealthmasters met the requirements placed on it in this case. I'll explain why.

There are several documents relating to Wealthmasters transaction with Mr W that are important to my consideration, these include the fact-finds, risk appetite questionnaire, and the suitability report.

I can see that Wealtmasters has raised an argument that Mr W is only complaining because some of his investments didn't work out. He's not brought a complaint about the switch of his pensions into a SIPP because he's satisfied with how everything else worked out. This is an important argument to consider because it wouldn't be fair if this Service essentially enabled customers to 'pick winners' after the event.

My starting point then was the broader transaction Wealthmasters undertook with Mr W. The advice to switch all three of his personal pensions into a SIPP and utilise the services of DFMs. Like the Investigator, I don't think its recommendation was unreasonable.

I note initially Wealthmasters was only advising Mr W to switch his OMW and AL plans because he was still receiving employer contributions to his group personal pension with SL. I think that position was sound, as was its later recommendation for him to switch all three pensions when it was confirmed he'd soon be leaving his employer and pension contributions would cease.

Wealthmasters found a significant element of Mr W's personal pension funds were over-exposed in terms of his assessed risk appetite, or were otherwise under-performing. So changes to his existing arrangements were required. And bearing in mind his pot exceeded £320,000, arguments in favour of a SIPP around consolidation, the flexibility offered by drawdown arrangements with his new provider and the ability to invest his total funds across a broader range of offers are satisfactory. In switching I can't see he lost any material guarantees or protections, or suffered such penalty.

The Greyfriars SIPP offered investment opportunities such as a DFM and structured products his previous pensions would be unlikely to accept and it offered simplified administration. The DFMs selected were well established. It seems Mr W wanted his funds actively managed to ensure they remained within his risk appetite. And while DFM arrangements often carry higher charges, returns to clients with larger portfolios can outweigh the additional charges.

I'm satisfied the advice to invest in the Brewin Dolphin and Sanlam portfolios was suitable in this case. And the SCARP appears to have been a suitable investment for Mr W's portfolio because it represented a modest portion of his funds; he had no immediate need for the funds at the time of the advice; the counterparties were four large UK financial services institutions; and he was prepared to accept some risk with his investments.

From Wealthmasters 2015 advice, that leaves the investments Mr W is complaining about.

Firstly I note that on the P6 application form from May 2015, it described Mr W's investment experience in the following terms:

"Help design and build structured products, years of experience in funds, unit trusts and financial services in general."

And then, in answering a question as to why unregulated investments would be suitable for Mr W, Wealthmasters recorded:

"He has dealt with financial service firms on marketing products and understands risk v reward and knows this is not a 'fund' but a high risk investment."

But the Investigator found:

"[Mr W's] previous investments were unit linked funds and although he may have previously dealt with financial services firms during his career, I don't agree this meant he was in a position to understand the risks involved. I've also seen no evidence of [his] supposed previous experience of designing and building structured products, but in any case, the P6 and Dolphin investments were completely different investments to these."

I've already noted that Wealthmasters failed to respond to the Investigator's view. It follows I've no evidence to substantiate what was included in the P6 application, and therefore based on the other evidence I do have such as the fact-find, I agree with the Investigator's findings on this point.

The Greyfriars P6 application form shows the portfolio consisted of five bonds where the underlying investments ranged from car parks to overseas hotel developments. These investments were unregulated, esoteric, difficult to value, lacked liquidity and were reliant on third parties. The Dolphin investment shared the same traits.

In July 2010 the FCA issued guidance about unregulated investments in a 'Good and Poor Practice report'. This contained examples of good practice in relation to unregulated investments, for example where a firm had robust controls in place and limited client exposure to 3% to 5% of their portfolios, where those clients had been assessed as being suitable for unregulated investments.

Further, Wealthmasters will have been aware that in June 2013 the FCA published an alert notifying firms it was to ban the promotion of UCIS to the vast majority of retail investors in the UK. The alert stated that the promotion of these riskier and complex fund structures would generally be restricted to sophisticated investors and high net worth individuals, for whom those products were more likely to be suitable.

And on 28 April 2014 the FCA published another alert which stated it believed:

''pension transfers or switches to SIPPs intended to hold non-mainstream propositions are unlikely to be suitable options for the vast majority of retail customers. Firms operating in this market need to be particularly careful to ensure their advice is suitable.''

''In the cases we have seen, customers' existing arrangements were invariably traditional pension plans invested in mainstream funds or final salary schemes, with the customer generally having no experience of non-mainstream propositions and many having very limited experience of standard investments."

"The new arrangements firms proposed were to transfer or switch the customers' pension funds to a SIPP, with a view to investment in non-mainstream propositions, which were typically unregulated, high risk and highly illiquid investments. Some examples of these investments are overseas property developments, store pods and forestry. Such transfers or switches are unlikely to be suitable for the vast majority of retail customers.''

The P6 and Dolphin investments should only form a small part of an adventurous, experienced investor's portfolio with the capacity to take risks with their funds. Wealthmasters had recommended Mr W place 23% of his pension provision in such. But he was assessed by it as a moderate risk investor who was approaching retirement. There's no evidence to show he had any experience of these types of investments. It had also noted he was neither a sophisticated investor nor high net worth individual.

The risk appetite strategy agreed with Mr W indicated he was only prepared to invest 20% of his pension funds in above average risk funds – the P6 and Dolphin investments exceeded that level of risk. His previous investments were unit linked funds and although he may have previously dealt with financial services firms during his career, I don't think this meant he was in a position to understand the risks involved.

So, I've concluded that Wealthmasters advice in 2015 for Mr W to invest in Greyfriars P6 and Dolphin was unsuitable. While it did provide risk warnings about the investments this doesn't provide it with cover for making inappropriate recommendations. It had a duty of care to Mr W and had to treat him fairly.

The 2017 Dolphin recommendation

I don't find it surprising that customers ATR evolves over time. This will usually relate to their circumstances, including their life stages. Wealtmasters conducted regular ATR assessments with Mr W and these suggested he was becoming less cautious with his funds:

- May 2015 – moderate (19/34)
- July 2017 – moderately adventurous (36/50)
- June 2018 – moderately adventurous (38/50)

Mr W's assessed ATR appears to have been on an upward drift. But there's little information about what drove this. And given this was a period when he was entering retirement, its arguable this was a time when he should be reducing his exposure, or at least maintaining his initial stance. There's little by way of explanation for this evolution of Mr W's ATR on file.

Another important aspect of assessing a client's risk outlook is to consider their capacity for loss. Wealtmasters did so for Mr W and concluded in the following terms:

"Your overall wealth is such that losing some of your investments and pensions will not affect your standard of living and therefore I am comfortable your agreed risk profiles and my recommendations are aligned with your circumstances and indeed capacity for loss.

I find this statement too general, ambiguous and unhelpful. What is the scale of loss that Mr W and his wife could afford to take without any impact on their standard of living in retirement? I do think Mr W and his wife had some capacity for loss, but I find Wealthmasters failed to effectively quantify this to help guide his decision making.

So, even if I take Mr W's apparently increasing appetite for risk at face value when considering Wealthmasters advice for him to invest a further £20,000 into Dolphin in 2017, I find this justification fails for several reasons. For example, he already had a significant exposure to this non-standard investment. And even with his supposed increased appetite for risk, its arguable the Dolphin holding exceeded his newly assessed risk level. This is especially the case when taking into account his capacity for loss.

So, I've concluded that Wealthmasters recommendation for Mr W to invest into Dolphin in 2017 was also unsuitable.

Putting things right

I'm upholding Mr W's case. So, he needs to be returned to the position he would've been in now - or as close to that as reasonably possible – had it not been for the failures which I hold Wealthmasters Financial Management Ltd responsible for.

If Wealthmasters had provided suitable advice, I don't think Mr W would've invested in Greyfriars P6 or Dolphin. So, subject to Mr W cooperating with Wealthmasters Financial Management Ltd to provide any information it requires to assess his loss fairly, it needs to provide redress to him using the following framework.

For the 2015 recommendations about the Greyfriars P6 and Dolphin Investments, Wealthmasters Financial Management Ltd must:

- Compare the performance of Mr W's investment with that of the benchmark shown below. If the fair value is greater than the actual value, there is a loss and compensation is payable. If the actual value is greater than the fair value, no compensation is payable.
- If there is a loss, Wealthmasters should pay into Mr W's pension plan, to increase its value by the amount of the compensation and any interest. Its payment should allow for the effect of charges and any available tax relief. It shouldn't pay the compensation into the pension plan if it would conflict with any existing protection or allowance.
- If Wealthmasters is unable to pay the compensation into Mr W's pension plan, it should pay the amount direct to him. But had it been possible to pay into the plan, it would've provided a taxable income. So, the compensation should be reduced to notionally allow for any income tax that would otherwise have been paid. This is an adjustment to ensure compensation is fair – 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 or expected marginal rate of tax at his selected retirement age. It's reasonable to assume he is likely to be a basic rate taxpayer at the selected retirement age, so the reduction would equal 20%. But if he would've been able to take a tax-free lump sum, this would apply to 75% of the compensation, resulting in an overall reduction of 15%.
- Provide the details of the calculation to Mr W in a clear, simple format.
- Income tax may be payable on any interest paid. If Wealthmasters considers its required by HMRC to deduct income tax from that interest, it should tell Mr W how much it's taken off. It should also 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 if appropriate.

Investment name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
P6 & Dolphin	Still exists but illiquid	FTSE UK Private Investors Income Total Return Index	Date of investment	Date of settlement	Not applicable

Actual value

This means the actual amount payable from the investment at the end date. If, at the end date, the investment is illiquid (meaning it cannot be readily sold on the open market), it may be difficult to find the actual value of the investment. So, the actual value should be assumed to be nil to arrive at fair compensation. Wealthmasters should take ownership of the illiquid investment by paying a commercial value acceptable to the pension provider. This amount should be included in the actual value before compensation is calculated.

If Wealthmasters is unable to purchase the investment the actual value should be assumed to be nil for the purpose of calculation. It may require that Mr W provides an undertaking to pay it any amount he may receive from the investment in the future. That undertaking must allow for any tax and charges that would be incurred on drawing the receipt from the pension plan. Wealthmasters will need to meet any costs in drawing up the undertaking.

Fair value

This is what the investment would have been worth at the end date had it produced a return using the benchmark. Any withdrawal, income or other distributions paid out of the investments 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 are a large number of regular payments, to keep calculations simpler, I'll accept if Wealthmasters total all those payments and deduct that figure at the end.

For the 2017 recommendation about the Dolphin investment Wealthmasters Financial Management Ltd must:

- Compare the performance of Mr W'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.
- Provide the details of the calculation to Mr W in a clear, simple format.

Investment name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Dolphin	Still exists but illiquid	FTSE UK Private Investors Income Total Return Index	Date of investment	Date of settlement	Not applicable

Actual value

This means the actual amount payable from the investment at the end date. If at the end date the investment is illiquid (meaning it couldn't 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 Mr W agrees to Wealthmasters taking ownership of the investment, if it wishes to. If it's not possible for it to take ownership, then it may request an undertaking from Mr W that he repays Wealthmasters any amount he may receive from the investment in future.

Fair value

This is what the investment would've been worth at the end date had it produced a return using the benchmark. Any withdrawal from the Dolphin 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 are a large number of regular payments, to keep calculations simpler, I'll accept if Wealthmasters total all those payments and deduct that figure at the end to determine the fair value instead of deducting periodically.

Why are these remedies suitable?

I've chosen this method of compensation because:

- Mr W wanted capital growth and was willing to accept some investment risk.
- The FTSE UK Private Investors Income total return index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is made up of a range of indices with different asset classes, mainly UK equities and government bonds. It's a fair measure for someone who was prepared to take some risk to get a higher return.
- Although it's called income index, the mix and diversification provided within the index is close enough to allow me to use it as a reasonable measure of comparison given Mr W's circumstances and risk attitude.

Award for distress and inconvenience

In addition, Wealthmasters Financial Management Ltd should pay Mr W £250 to recognise the inconvenience its failings have caused him.

Further information

There is guidance on how to carry out calculations available on our website, which can be found by typing 'compensation for investment complaints' into the search bar on our website: www.financial-ombudsman.org.uk.

My final decision

For the reasons I've already set out, I'm upholding Mr W's complaint and I require Wealthmasters Financial Management Ltd to put things right in the way I've outlined.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 9 January 2023.
Kevin Williamson
Ombudsman