DRN-3748838

The complaint

Mr A complains that he was given poor advice by Sterling Wealth Ltd to transfer pension funds into a portfolio which was unsuitable and as a result has suffered a loss.

What happened

In 2013 Mr A's then independent financial adviser ("IFA") assessed his attitude to investment risk at level 7 (medium to high). This was reviewed in May 2014, at which time he placed himself as a moderate risk taker.

In December 2014, Mr A approached his adviser for recommendations in relation to a £40,000 sum he had received from some investments that had matured. He said his thinking was to invest £25,000 at medium risk, where the capital would be protected, and £15,000 at higher risk.

In April 2015, a memorandum of understanding was signed between the IFA and Sterling Wealth. They agreed that all of the IFA's clients would be transferred to Sterling Wealth by way of novation, and Sterling Wealth would take ownership of the clients. Under the terms of the agreement the previous adviser would work as a consultant for Sterling Wealth until both parties felt that management of the clients could be handed over.

In May 2015, the previous IFA wrote to Mr A advising that, following a review of the investment platform market, he was recommending that Mr A transfer his Individual Savings Account ("ISA") and pension holdings to a new platform, saying access to a Discretionary Management Service, accessing some particular investments, was the main reason for transferring.

A recommendation was made that Mr A invest 30% in an alternative portfolio, with the balance of 70% invested into one of the managed portfolios (the latter being in line with how he was currently investing).

Under the heading: *'What service can I expect going forward?'* the letter said: *'You will receive quarterly reviews with recommendations to rebalance and to possibly switch some of the funds.*

The transfer authority and discharge forms were sent in June 2015.

The IFA wrote to Mr A advising him that it had decided to merge its clients with those of Sterling Wealth.
Mr A's pension funds were transferred to the new platform in July 2015. In August 2015 the provider cancelled the previous IFA's agency, and recorded Sterling Wealth as Mr A's adviser.

On 28 August 2015, the provider wrote to Sterling Wealth confirming that switch instructions to the new portfolio ("P6 portfolio") had been executed with an application date of 20 August, and in accordance with those instructions a number of trades were placed.

On 30 August 2016, additional trades of £9,400 were placed. Again, confirmation was sent by Sterling Wealth.

In February 2019 the Financial Services Compensation Scheme ("FSCS") started accepting claims relating to the portfolio as some of the non-standard investments had become illiquid, meaning they couldn't be sold or traded. Mr A asked the FSCS to investigate a claim against his previous IFA for unsuitable advice to invest in that portfolio. The FSCS rejected that claim, on the basis that the first purchase didn't happen until 27 August 2015, so it could only have been performed by Sterling Wealth, which was still trading.

Mr A complained to Sterling Wealth, which sent its final response in March 2021, saying it didn't agree with the FSCS decision as it wasn't responsible for the advice to invest in the portfolio – that advice having been given by the previous IFA. Sterling Wealth said it had not taken on the previous IFA's liabilities. So Mr A brought his complaint to this service.

Our investigator thought the complaint should be upheld. He said Sterling Wealth had taken on responsibility for Mr A and, as the funds were invested in the portfolio after this happened, it was responsible for this – even though the original advice to transfer had been given by the previous IFA.

The investigator asked Sterling Wealth to carry out a calculation to establish if Mr A has suffered a loss and, if he has, to compensate him for that loss. He also recommended that it pay compensation of £250 for the distress and inconvenience caused to him by the uncertainty over the potential losses.

Sterling Wealth did not accept the investigator's findings and so the complaint has been referred to me to make 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.

The advice to invest some of Mr A's funds in the portfolio was given by the previous IFA. However, by the time the transactions took place Mr A was a client of Sterling Wealth. So I agree Sterling Wealth was responsible for the transactions proceeding. By that date, Sterling Wealth was noted as Mr A's IFA and it gave the instructions for the transactions to go ahead. Sterling Wealth took on the previous IFA's clients following an agreement said to be by way of novation – which generally means that the existing contract continues, but with a new party taking the place of one of the original parties. In this case, that meant Sterling Wealth took the place of the previous IFA.

Sterling Wealth says it didn't give Mr A advice, and shouldn't be responsible for the actions of another firm. The advice may have been given by the previous IFA but, as I've explained, by the time the transaction took place Mr A was Sterling Wealth's client. Sterling Wealth has argued that it didn't take on any liabilities of the previous firm but it hasn't provided evidence to confirm this. Based on the information I have, I'm satisfied Sterling Wealth is responsible.

I would expect an IFA taking on a new client to review the client's circumstances within a reasonable time, looking at their existing investments and taking into account the client's attitude to risk. Sterling Wealth's terms of business say it will offer an initial discussion, and gather information about the client's circumstances and their aims and objectives, before making recommendations.

In this case, Mr A didn't have a review until 2017. By not reviewing his circumstances at the time, Sterling Wealth missed the opportunity to advise on the suitability of his investments. It could have reviewed whether this would be suitable for Mr A but instead went ahead with instructions to place the new trades without having reviewed this. The online platform has confirmed that the purchases were instructed by Sterling Wealth, which was the adviser holding the agency.

When Mr A sought recommendations for £40,000 he had available to invest in December 2014, his funds were invested in a number of regulated pooled investments, providing what I'd consider a balanced risk portfolio.

That investment approach was consistent with the latest risk assessment, in May 2014, where Mr A placed himself as a moderate risk taker. He said he wished to split the new investment with 62.5% being capital protected and 37.5% at a higher risk level. I would consider this to be a medium risk approach.

Mr A was advised to switch to the new platform in order to access a particular portfolio (the P6 portfolio). This portfolio is a discretionary managed investment portfolio offering access to mini bonds. These are short-term loans to smaller businesses, which can't be traded on the stock market and are not covered by the FSCS. As they include unregulated investments in overseas commercial property, I wouldn't consider them to be suitable for someone with a moderate risk tolerance.

Mr A was advised to invest 30% of his pension portfolio into this portfolio. The FCA 'Unregulated Collective Investment Schemes: Good and poor practice' report 2010 gives an example of good practice when advising sophisticated, high net worth individuals, limiting investment in unregulated investments to no more than 3%-5% of the portfolio, with this being backed-up by robust and on-going due diligence and monitoring. Sterling Wealth should have been aware that a much higher proportion of Mr A's pension fund would be invested into these unregulated funds – well above the proportion recommended.

I don't consider this was suitable for Mr A, who didn't fit the profile of the limited group of sophisticated high net worth investors for whom unregulated investments may be suitable. On that basis, I think it was unsuitable. And as I've explained, Sterling Wealth was responsible for facilitating this. So the complaint should be upheld.

Putting things right

In assessing what would be fair compensation, my aim is to put Mr A as close as possible to the position he would probably now be in if he had been given suitable advice.

It's my opinion the advice to transfer was designed to facilitate the investment into the portfolio described above. I think that had Mr A received suitable advice to remain with his previous provider, he would have accepted that advice. As Sterling Wealth was responsible for actioning the investment transactions, it should have realised they were unsuitable and reviewed the previous advice given at that point. I'm satisfied that what I have set out below is fair and reasonable in this situation.

- Any loss Mr A has suffered should be determined by obtaining the notional value of the pension if it had been with the previous provider, and subtracting the current value of the pension from this notional value. If the answer is negative, there's a gain and no redress is payable.

- The compensation amount should if possible be paid into Mr A's pension plan. The payment should allow for the effect of charges and any available tax relief. The compensation shouldn't be paid into the pension plan if it would conflict with any existing protection or allowance.

- If a payment into the pension isn't possible or has protection or allowance implications, it should be paid directly to Mr A as a lump sum after making a notional reduction to allow for future 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 A won't be able to reclaim any of the reduction after compensation is paid.

- The notional allowance should be calculated using Mr A's actual or expected marginal rate of tax at his selected retirement age.

- If Mr A hasn't yet taken any tax-free cash from his plan, 25% of the loss would be tax-free and 75% would have been taxed according to their likely income tax rate in retirement – presumed to be 20%. So making a notional reduction of 15% overall from the loss adequately reflects this.

- In addition, Sterling Wealth should pay Mr A £250 for the level of distress and inconvenience caused to him

- Sterling Wealth should provide the details of the calculation to Mr A in a clear, simple format.

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

Portfolio name	Status	Benchmark	From	To	Additional interest
Novia pension P6 portfolio	Some liquid/some illiquid	Notional value from previous provider	Date of Disinvestment from previous provider	Date of settlement	8% simple per year from the date of my final decision to the date of payment (if not settled within 28 days of the business receiving the complainant's acceptance)

Actual value

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

If, at the date of settlement, any residual investment is illiquid (meaning it can't 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.

Sterling Wealth should take ownership of the illiquid investment by paying a commercial value acceptable to the pension provider. The amount Sterling Wealth pays should be included in the actual value before compensation is calculated.

If Sterling Wealth is unable to purchase the illiquid investment the actual value should be assumed to be nil for the purpose of calculation. It may wish to require that Mr A 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. Sterling Wealth will need to meet any costs in drawing up the undertaking.

Notional Value

This is the value of Mr A's investment had it remained with the previous provider until the end date. Sterling Wealth should request that the previous provider calculate this value. Any additional sum paid into the pension should be added to the notional value calculation from the point in time when it was actually paid in.

Any withdrawal from the pension paid to Mr A should be deducted from the notional 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 the total of those payments being deducted at the end to determine the notional value instead of deducting periodically.

My final decision

My final decision is that I uphold the complaint and direct Sterling Wealth Ltd to pay the fair compensation set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 9 November 2022.

Peter Whiteley
Ombudsman