DRN-3998023

The complaint

Mr E says that advice given by Berkeley Financial Partners (BFP) about his pension – to transfer to a new SIPP (self invested personal pension) and invest via a Discretionary Fund Management (DFM) arrangement – was unsuitable.

BFP was and remains an appointed representative of FACET Investment Management Ltd (FACET). As the principal, FACET is responsible for the advice BFP gave. For convenience I've just referred below to FACET which should be taken to mean BFP as appropriate.

What happened

In 2016 Mr E was aged 59 and employed full time, earning around £45,000 pa. He had a SIPP with Standard Life. He'd taken the full amount of tax free cash in 2012 to repay his mortgage. He was also a member of his employer's GPP (Group Personal Pension) into which contributions of 14% of his salary were being made. His SIPP, valued at £130,225, was invested across four of the provider's funds: two managed funds made up nearly 57%, with a further 32% or so in an equity fund and about 11% in a corporate bond fund. An attitude to risk (ATR) questionnaire indicated Mr E was a medium risk investor (4 out of 6).

FACET's suitability report dated 29 August 2016 recommended that Mr E switch to a Standard Life platform SIPP and invest using FACET's DFM service. FACET Fund no 3 was recommended. The report noted that the annual ongoing charge was '*marginally higher*' than Mr E's existing arrangement.

Mr E accepted the recommendation. My understanding is that FACET Fund no 3 was made up of holdings in the FACET Cautious and FACET Balanced Funds. Both Funds were suspended in 2019. And in 2020 it was confirmed that the Funds would be wound up and the money realised returned to investors. But some of the holdings were illiquid and couldn't be sold.

In 2020 Mr E's employment came to an end. Mr E completed a fact find and ATR questionnaire in March 2020 and was reassessed as a low risk investor. In April 2020 the accumulated value of his GPP was switched into his SIPP. There was a review meeting in June 2021. Mr E amended his ATR to lowest medium and switched to a lower risk portfolio.

In June 2022 Mr E complained to FACET about the advice he'd been given. Mr E said his portfolio had lost a significant amount which he believed was because too much had been invested in a single illiquid and high risk investment. Mr E also thought the portfolio was generally higher risk than his ATR.

FACET didn't uphold the complaint. FACET said the advice was suitable as the portfolio, as a whole, was within the applicable risk profile. FACET did offer to waive some of its charges.

Mr E referred his complaint to us. It was considered by one of our investigators who upheld it. He referred to the 2008 report issued by the then regulator entitled '*Quality of advice on pension switching*' and to some of the examples given as to what might constitute unsuitable advice, which included where extra product costs were incurred without good reason. The costs of Mr E's existing SIPP weren't detailed but the suitability report confirmed the costs of the new arrangement were higher. So there'd need to be a good reason for Mr E to switch. The investigator wasn't persuaded that was the case. His main reasons were:

- The switch recommendation was primarily based on the suggestion the DFM arrangement could reduce volatility. FACET explained in the suitability report that reduced investment volatility was '…*one probable outcome of a discretionary management service*'. But there was no guarantee of that.
- FACET said the existing SIPP portfolio matched someone with a higher medium risk profile, or one place higher than Mr E's medium ATR. FACET also noted that the existing provider had other funds available, saying: '*As well as accommodating the discretionary fund management facility, Standard Life offers an extremely wide range of both in-house and external investment funds'*. Given there was no guarantee of reduced volatility, or improved performance from the DFM arrangement, which also came at a higher cost, FACET should've investigated reducing the level of risk by switching funds within Mr E's existing SIPP.
- Mr E's recollection was that he was approached by FACET with the DFM proposal, rather than he himself seeking a change or, in particular, a DFM service. He was a relatively inexperienced investor who didn't require a DFM arrangement.
- Any perceived benefits from switching to the DFM arrangement didn't outweigh the additional costs, with no specific guarantees of Mr E being better off as a result, especially when alternative reduced risk options were available under his existing set up. The recommendation to switch to a DFM was unsuitable.
- Under a DFM arrangement, the investor is meant to be invested in assets aligned to their risk profile. In this case, the DFM arrangement ultimately exposed Mr E to assets that suffered liquidity issues and caused financial loss. It seemed one fund manager was '…*given a free hand as to where to invest and when, and also in respect of the quantum of purchases and sales'*. This in itself had increased the level of risk.

FACET didn't accept the investigator's view and referred to a recent final decision issued by one of our ombudsmen. FACET said some of the investigator's comments were inconsistent with that decision. In summary FACET made the following points:

- The investigator's view implied a need for the sought after benefits to be guaranteed. That was irrational. Only in very limited scenarios would there ever be guaranteed outcomes. Reduced volatility or improved performance couldn't be guaranteed. Approaches could be taken aimed at reducing volatility but that was never guaranteed and wasn't a reason to suggest a solution was unsuitable.
- The fact that the Funds ultimately suffered difficulties didn't mean they were unsuitable at the time of the advice or that could've been known at the time. FACET quoted extracts from the other ombudsman's final decision in support.
- FACET agreed there'd need to be good reason for switching if the cost of the new arrangement was more. FACET pointed to Mr E's objectives. He wanted to move to an ongoing service. The solution provided that. Just switching funds within the existing SIPP failed to take into account that the cost would increase because Mr E wanted ongoing advice.
- The increased cost was addressed in the suitability report. The ombudsman in the other case had noted that there was sometimes more than one product or approach which might meet the consumer's circumstances and objectives. Another adviser might take a different approach but that didn't mean the advice and the suggested solution wasn't suitable.

The investigator considered FACET's comments but he maintained FACET's advice was unsuitable. The investigator made the following points:

- He hadn't said Mr E required or expected a guaranteed income. On balance the investigator didn't think the move to a DFM was warranted, given the uncertainty of Mr E being better off, especially when the starting point was a higher cost.
- The investigator remained unconvinced that a portfolio invested in assets that were so susceptible to pricing and liquidity issues could be deemed suitable for a medium risk investor and one who wanted to take a more cautious approach with less volatility. And, given the ongoing advice arrangement, it was FACET's responsibility at outset, and ongoing, to ensure the suitability of the investments for Mr E.
- With reference to what had been said in the other decision about more than one product or approach being suitable, FACET hadn't considered if Mr E could achieve his objectives by switching funds within his existing SIPP.

FACET disagreed and asked for the complaint to be referred to an ombudsman. Amongst other things, FACET said events after the advice had been given, or the ultimate performance of the funds, weren't relevant to determining if the advice was suitable at the time it was sought. What the ombudsman had said in the other final decision was set out – that the later issues experienced with the Funds didn't mean the recommendation in 2016 was unsuitable. The investigator had referred to pricing and liquidity issues. But, unless those should've been known at the time of the advice, that was with the benefit of hindsight.

FACET also cited what the Court of Appeal had said in a case involving this service – that like cases should be treated alike, that consistency was required; and arbitrariness on the part of the ombudsman, including an unreasoned and unjustified failure to treat like cases alike, would be a ground for judicial review. FACET said that whether the suspension and liquidity problems should've been in FACET's reasonable knowledge and whether the model portfolios were a certain level of risk were both questions of fact. Deciding those factual points differently would be in breach of what the Court of Appeal had said.

The investigator responded. He said the opportunity for growth decreased with a lower risk profile and so lower risk investments were arguably more sensitive to cost because the opportunity for growth is less. So it seemed counter intuitive to reduce the potential for growth but increase the costs. The investigator maintained that Mr E's pension fund could've been switched within the existing SIPP to lower risk funds with or without ongoing advice. It had been an adviser led decision to go into the DFM. The investigator wasn't persuaded that advice had been in Mr E's best interests.

The investigator told FACET and Mr E that, as agreement hadn't been reached, the complaint would be referred to an ombudsman to decide.

FACET added that what the investigator had said might be true when dealing with very low risk mandates. But where, as in this case, the investment risk was medium, the notion that a DFM service will be too expensive to be worthwhile (again as a default position) is entirely misplaced. FACET said the investigator's focus had been on cost. That's an important consideration but there are other factors. The use of a DFM was to further the client's objectives. In that light and relying on its previous responses, FACET maintained it was incorrect to conclude the advice and using a DFM in Mr E's case was unsuitable.

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.

I've read and considered everything. I've paid particular attention to what FACET has said about why it doesn't agree with the investigator's view. But my findings focus on what I see as the key issues.

FACET has made several references to a final decision issued by another ombudsman. I'm not bound by another ombudsman's decision. We aim for consistency but we decide cases on their individual facts and merits. Complaints which might appear similar may result in different outcomes. Although the final decision FACET has pointed to wasn't an uphold, I've seen that we've issued other final decisions upholding complaints which aren't dissimilar to Mr E's. I think that underlines our approach of deciding each case on its particular facts. FACET has also referred to what it considers are findings of fact and which FACET says should be consistent. But my decision in Mr E's case doesn't turn directly on either of the issues FACET has pointed to.

I agree with the investigator and the reasons he gave as to why Mr E's complaint should be upheld. I don't think FACET's advice was suitable for Mr E. Essentially, Mr E had no real need to switch to a new SIPP. Nor do I think a DFM was necessary or suitable for Mr E. And, if Mr E hadn't been advised to switch so that he could avail himself of the DFM arrangement, he wouldn't have been exposed to the two Funds that were eventually wound up with illiquid assets. I agree that Mr E could've been instead advised to switch and diversify funds within his existing SIPP.

FACET has argued very strongly that the recommended solution presented advantages. And that it enabled Mr E to meet his objectives. Particularly in terms of the provision of ongoing advice and monitoring.

The recommendation in the suitability report was said to meet Mr E's objectives of '*potentially higher returns via a more "targeted" and consistent investment approach, coupled with a product that offers all of the latest "facilities" in regard to investment and future income provision.*'

I don't see that's consistent with what had been recorded about Mr E's objectives earlier on in the suitability report. It said that Mr E wanted to retire at age 66 (so in seven years' time); he was concerned with recent volatility; going forwards, didn't want to take any unnecessary risks with his pension plan as it had taken a long time to build up; and he'd like to start having annual reviews. FACET also noted that Mr E's current investments were consistent with a higher medium ATR whereas Mr E's ATR was medium. So, overall, Mr E was looking to take a more cautious approach, consolidate earlier gains and have the benefit of an annual review.

I don't see why those aims dictated a switch to a new product with a DFM. The suitability report noted that Standard Life offered '*an extremely wide range of both in-house and external investment funds'*. Mr E's existing portfolio could've been rebalanced to reflect a more cautious approach with lower volatility and some potential for growth going forwards. Like the investigator I don't think there's any evidence that FACET explored whether the funds available to Mr E under his existing arrangement could've been utilised. Much less discounted that solution and explained why it wasn't suitable to Mr E.

FACET has pointed largely to the availability of the DFM with the new arrangement and the facility for ongoing advice. I think Mr E's need for ongoing advice could've been met differently – for example by way of an annual review. Which is what Mr E had said he wanted. The suitability report records he'd '*specifically like to start undergoing annual reviews to check on the performance of the pension and understand what options are available*' to him. If Mr E's fund had been switched into more cautious funds with his existing provider I don't see there'd have been a need for ongoing monitoring or more frequent review than annually. Mr E would've incurred advice fees but he'd confirmed he was prepared to pay for an annual review service. There was no need to switch to a new product and a DFM in order to meet the requirement for periodical review.

It isn't disputed that the suitability report said that the charges for the new arrangement would be more. Although, as the existing charges weren't set out, Mr E couldn't see exactly how much more he'd be paying. I agree that the cheapest solution isn't always the best one. And, as I've said, Mr E would've incurred extra costs if an annual review had been incorporated. But FACET agrees that, where higher costs will result, those costs need to be justified. FACET said that '*any additional costs for the discretionary managed portfolio should be more than offset by both better performance and lower volatility coupled with the positive impact that the latter is likely to have on future regular income withdrawals*'. I don't find that statement persuasive. I don't see any real reason why it would be expected that the new arrangement would perform better or experience lower volatility.

I don't agree that the investigator's view was on the basis that the benefits under the new arrangement should've been guaranteed. I think all the investigator was saying was that there'd need to be a reasonable prospect that improved retirement benefits would result which the investigator didn't think was the case. That's my view too.

I'm not convinced that the switch to a DFM arrangement was necessary or justified in Mr E's case. His pension fund was modest and I think he could've maintained his existing SIPP and switched to lower risk funds which could've been annually reviewed. Mr E wasn't an experienced or knowledgeable investor. His existing provider offered a wide range of funds. I don't think Mr E needed access to a DFM.

And introducing a DFM meant Mr E's pension fund was potentially exposed to higher risk investments. The DFM had a very wide investment mandate – the recommendation letter refers to the DFM as having a '*free hand as to where to invest and when*'. I don't think that's quite the case – the DFM will usually rely on information from the adviser such as the client's ATR and the DFM's selection of assets or portfolio must be consistent with that – but the level of discretion the DFM had potentially increased the degree of risk for Mr E.

That's borne out by what actually happened. Some of the investments selected by the DFM did encounter difficulties and subsequently failed. I'm not sure that FACET is entirely right when it says that what happened to those investments couldn't have been foreseen and so the benefit of hindsight has been used. Given the very wide discretion the DFM had and which FACET recognised from the outset, arguably it was always possible and foreseeable that the DFM could invest in the selected assets.

But whether that's right or not, I don't agree with FACET that events after its advice was given aren't relevant. Regardless of what actually happened with the investments and if it was foreseeable, if FACET hadn't advised Mr E to invest via the DFM, Mr E wouldn't have been invested as he was and he wouldn't have incurred the losses he did. Mr E's losses flow from the recommendation to use a DFM which I've said was unsuitable.

Overall I'm not persuaded that switching Mr E's SIPP into a new SIPP with the same provider and entering into a DFM arrangement was in Mr E's best interests. I think it exposed him to a more expensive and complicated arrangement which wasn't necessary to meet his objectives and which arguably carried more risks than Mr E wanted or could tolerate.

Putting things right

In assessing what would be fair compensation, my aim is to put Mr E as close as possible to the position he'd probably now be in if he had been given suitable advice. I think Mr E would've retained his existing SIPP but switched into lower risk funds. I can't be certain precisely what investments he would've made instead. But on the basis he wanted to take slightly less risk, I'm satisfied that what I've set out below is fair and reasonable given Mr E's circumstances and objectives when he invested.

What should FACET do?

To compensate Mr E fairly FACET should:

- Compare the performance of Mr E's investment with the benchmark shown below. If the actual value is greater than the fair value, no compensation is payable. If the fair value is greater than the actual value, there is a loss and compensation is payable.
- Add any interest set out below to the compensation payable.
- If there's a loss it should be paid into Mr E's pension plan, to increase its value by the amount of the compensation and any interest. The payment should allow for the effect of charges and any available tax relief. The compensation shouldn't be paid into the compensation into the pension plan if it would conflict with any existing protection or allowance.
- If FACET is unable to pay the compensation into Mr E's pension plan, it should pay that amount direct to him. But had it been possible to pay into the plan, it would've provided a taxable income. Therefore the compensation should be reduced to notionally allow for any 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 E won't be able to reclaim any of the reduction after compensation is paid.
- The notional allowance should be calculated using Mr E's actual or expected marginal rate of tax at his selected retirement age. It's reasonable to assume Mr E is likely to be a basic rate taxpayer at the selected retirement age, so the reduction would equal 20% as this element of his pension had been fully crystallised.
- Pay Mr E £300 for the distress and inconvenience caused by the unsuitable recommendation and the ongoing uncertainty around the value of his pension and how this might affect him in the future.
- Provide the details of the calculation to Mr E in a clear, simple format.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Standard Life SIPP	Some liquid/some illiquid	FTSEUK Private Investors Income Total Return Index	Date of transfer	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, any investment in the portfolio is illiquid (meaning it cannot be readily sold on the open market), it may be difficult to find the actual value of the portfolio. So, FACET should take ownership of any illiquid investments within the portfolio by paying a commercial value acceptable to the pension provider. This amount paid should be included in the actual value before compensation is calculated.

If FACET is unable to purchase any illiquid investment the value of that investment should be assumed to be nil when arriving at the actual value of the portfolio. FACET may wish to require that Mr E provides an undertaking to pay FACET any amount he may receive from that investment in the future. The undertaking must allow for any tax and charges that would be incurred on drawing the receipt from the pension plan. FACET 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 additional sum paid into the investment should be added to the fair value calculation from the point in time when it was actually paid in. Any withdrawal from the Standard Life SIPP 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 is a large number of regular payments, to keep calculations simpler, I'll accept if FACET totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically.

Why is this remedy suitable?

I've chosen this method of compensation because Mr E wanted if possible some capital growth and was willing to accept some investment risk. I note Mr E's ATR to risk changed in 2020 and 2021. But I think that was largely in response to what had happened and a reaction to the losses he'd incurred. Otherwise I think he'd have maintained the same medium ATR throughout. So I think it's fair to use the same benchmark throughout.

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 is 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 E's circumstances and ATR.

My final decision

I uphold the complaint. FACET Investment Management Ltd must redress Mr E as I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr E to accept or reject my decision before 12 June 2023.
Lesley Stead
Ombudsman