

The complaint

Ms L complains that she was advised by Inter-UK Financial Services Limited (“IUK” or “Inter-UK”) to switch her two existing personal pensions (PPs) to a Self-Invested Personal Pension (SIPP). The recommended portfolio held some investments that either failed or became illiquid and Ms L lost money as a result. Ms L was also unable to access her pension for a long time. She would like to be reinstated to the position she would have been in if not for the advice.

What happened

Ms L wanted advice on her two PPs, which were both invested in With-Profits funds. The total value of the two pensions was around £171,000.

At the time Ms L was self-employed and owned her own home with no mortgage. Aside from the two pensions she had about £100,000 in savings. She wanted to reduce the hours she worked in a few years, but to maintain her income. IUK recorded Ms L as having a ‘Balanced to Adventurous’ risk profile.

IUK recorded in its fact-find with Ms L that she wanted ‘control and flexibility’ with her pensions and to be able to continue to make contributions while she was working. She was concerned about charges and whether she would be better off with just one pension rather than two and wanted to know that someone was managing her fund.

IUK carried out some analysis then advised Ms L to transfer both PPs into a SIPP with the underlying funds managed by SVS Securities, a Discretionary Fund Manager (DFM), in their Mixed Portfolio. The funds were transferred and invested mainly in direct equities and unlisted bonds.

SVS were later placed into administration following serious concerns on behalf of the Financial Conduct Authority over how the business was run. SVS had invested client funds, including Ms L’s, in a number of high risk, illiquid securities, many of which later became worthless (the unlisted bonds).

Ms L complained to IUK in July 2021, after two years spent trying to get her money back. Although IUK acknowledged the complaint no final response was issued. But Ms L says that a director of IUK told her by telephone in October 2021 that the complaint would be upheld and compensation offered in due course.

By May 2022 the director emailed Ms L to say that he was still trying to calculate compensation, but no offer or payment has yet been received. Ms L brought her complaint to this service where our investigator upheld the complaint.

Since IUK did not respond, the case was referred to me for a final 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.

I have to decide whether the advice by IUK to transfer was suitable. COBS 9 of the FCA's handbook applies when regulated businesses give advice on pensions and investments, like IUK did here. So I have carefully considered whether they met the requirements there. Key sections are:

COBS 9.2.1R:

'(1) A firm must take reasonable steps to ensure that a personal recommendation, or a decision to trade, is suitable for its client'.

COBS 9.2.2R:

'(1) A firm must obtain from the client such information as is necessary for the firm to understand the essential facts about him and have a reasonable basis for believing, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of managing:

- (a) meets his investment objectives;*
- (b) is such that he is able financially to bear any related investment risks consistent with his investment objectives; and*
- (c) is such that he has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.*

COBS 9.4.7R:

"The suitability report must, at least:

- (1) specify the client's demands and needs;*
- (2) explain why the firm has concluded that the recommended transaction is suitable for the client having regard to the information provided by the client; and*
- (3) explain any possible disadvantages of the transaction for the client."*

So in order for IUK's advice to be suitable it had to meet these requirements.

One of Ms L's concerns was whether she would be better off combining her pensions. She also wanted as much income as possible.

IUK's analysis dated 12 April 2018 shows that the recommended SIPP and SVS portfolio was more expensive than both of the existing schemes. The projected fund value at age 66 with the existing PPs, based on the medium return illustration, was £224,210. The projection for the pension fund in the recommended SIPP, based on the same returns, and excluding ongoing adviser charges was £168,000. Even the projection for higher returns only achieved £206,000 in the SIPP.

So IUK's recommended switch had to significantly outperform the highest illustration provided. And I would normally only expect customers willing to take on high risk investments to be able to consistently receive investment returns at or above the higher industry projected rates. But IUK also recommended an ongoing advice service, building in yet another charge and making it even more likely that Ms L's pension fund would be worth less following its recommendation.

For this recommendation to be suitable, IUK had to show why the higher costs were justified. But the higher costs were not discussed in the suitability report and there is no evidence that

Ms L and her adviser discussed the analysis that IUK had carried out. While the SIPP would give Ms L the flexibility she wanted, that alone did not justify the higher costs. And there is no evidence that IUK carried out any performance analysis of its recommended DFM. There is nothing in the suitability report to show why IUK believed that the SIPP/SVS portfolio would outperform, or that the level of additional cost was even disclosed. On the whole I think that IUK's recommendation was very likely to leave Ms L with a smaller pension fund in retirement.

Furthermore, the larger of Ms L's two pensions (with Standard Life) offered a guaranteed growth rate of 4% a year. And had preferential charges of 0.2%. As with the costs, this was not disclosed in the report and there is no evidence that the benefit of these things was discussed.

In addition, and also not disclosed or discussed, the SVS portfolio held about 40% in potentially illiquid investments. But Ms L was intending to access her fund within a few years. This meant there was a risk that Ms L would not be able to sell some of her investments when she needed to withdraw money from her pension.

So I find that the recommendation to transfer to the SIPP did not meet Ms L's objectives of reducing costs and maximising income. The report did not explain why IUK believed the advice to be suitable, nor did it explain the possible disadvantages of the recommendation. IUK therefore did not meet the requirements of COBS 9.2.2R and COBS 9.4.7R.

IUK had to ensure the recommended portfolio met Ms L's attitude to risk. There is some conflicting information in the file over Ms L's assessed risk score. The questionnaire recorded a score of 46 (although when correctly calculated the score was 48); but the report said the score was in the range of 53 to 65 from a potential score of 19 to 66. The questionnaire showed a range of scores from 0 to 66+.

Despite this the description of the risk profile was consistently given as Balanced to Adventurous. Ms L later said that she thought her risk profile would be accurately described as medium. Some of the questions relate to capacity for loss and knowledge and experience of investing. But the responses to questions 5 to 9, which explore her willingness to take risk, show that Balanced to Adventurous is a broadly reasonable description of the level of risk Ms L was willing to take.

The resulting portfolio that SVS constructed, based on the statement on file, was much higher risk than that. Some 40% of the portfolio was in high risk potentially illiquid unlisted bonds. And this part of the portfolio was poorly diversified, with just over half of it from a single issuer. Apart from uninvested cash the rest was in equities, including higher risk smaller companies. I don't think that Ms L was willing to take this level of risk with her pensions.

I also think Ms L had a fairly low capacity for loss in respect of these two pensions. The total value was £171,000 and she had about £100,000 of other savings. Ms L wanted to maintain a high income in retirement of 'as much as it could be.' Based on her expenditure questionnaire this would mean just under £3,000 a month. While this meant that Ms L would have to accept some risk, it also meant that she was reliant on her pensions for her retirement income. Also, she was intending to start taking benefits in a relatively short period of time.

And as I have already said about 40% of the portfolio was high risk and potentially illiquid, with about half from a single issuer. So if this issuer failed, Ms L was facing the loss of 20% of her whole pension. Given her relatively short term to retirement and level of contributions she would have little opportunity to allow her fund to recover from the potential losses from

investing in this way.

Ms L described herself in the questionnaire as “not very familiar when it comes to investments.” Her two existing pensions were invested in the With Profits funds, and the rest of her savings was in cash so there was no evidence that she had previously invested in non-mainstream or direct investments.

So I find that the recommended solution was higher risk than Ms L was willing to take, and was also higher risk than she could afford to take. Furthermore the risks of direct investment into smaller companies and potentially illiquid investments were not explained to Ms L in her suitability report, so I don’t think she was aware of the level of risk she was taking. And I don’t think Ms L had sufficient knowledge and experience of investing to understand these risks even if they had been explained to her.

So IUK did not meet the requirements of COBS 9.2.2R and COBS 9.4.7R.

So I find that IUK’s recommendation to switch from her PPs to the SIPP and DFM portfolio was unsuitable for the reasons given above.

IUK may say that they did not know that SVS would be investing in the high risk, potentially illiquid investments.

But IUK gave the recommendation to invest in the SVS portfolio. They were required to take reasonable steps to ensure that the portfolio was suitable. That meant finding out about the underlying investments. If they didn’t do that (and there is no evidence they did) they would not have been able to determine whether the transaction as a whole was suitable, and would therefore not have met the requirement at COBS 9.1.1R.

I understand that IUK might take the view that SVS are also responsible for some of the losses. Although SVS were responsible for the individual investment decisions, IUK recommended the SVS portfolio service, so were responsible for ensuring it was suitable. Ms L remained a client of IUK, relying on their advice. I can see no evidence that Ms L would ever have invested with SVS if not for IUK’s advice.

Furthermore there is no evidence that IUK ever advised Ms L that the SVS portfolio was unsuitable, and in the absence of such advice Ms L was entitled to believe that it was suitable. If SVS had stepped outside of their remit in the types of investment, IUK would or ought to have known when carrying out the reviews as described in their service proposition.

In any case, I have already explained that the advice was unsuitable because of the increased costs which were not justified and because Ms L did not have the knowledge and experience necessary to understand or need the services of a DFM.

I think it’s important to clarify that I’m not saying IUK is wholly responsible for the losses simply because SVS Securities is now in liquidation. I have explained above why I have found that IUK’s advice was unsuitable, notwithstanding any wrongdoing by SVS. But for that unsuitable advice, Ms L’s pension would, more likely than not, have been in a personal pension in a mainstream medium risk investment portfolio. She would never have been placed into a position where she was exposed to the types of financial risk that she was but for IUK’s mistake. So I think it is fair and reasonable that IUK should take full responsibility for Ms L’s losses as a result of its advice.

It is clear that Ms L was looking to review her pensions and make some changes. It is not clear exactly what she would have done but I think that if she had been given suitable advice, she would have changed providers to another PP that offered flexible access without

the additional costs and risks of a DFM. I think she should have been advised to invest in a medium risk portfolio, taking into account her assessed risk profile and relatively low capacity for loss. But in fairness to IUK Ms L would still have taken advice on her pension so I am not going to require them to refund the initial fee because she would have had to pay a fee in any case.

In summary I find that IUK's advice was unsuitable as their recommendation caused Ms L to incur higher charges and did not match her risk profile or capacity for loss.

Ms L has been attempting to resolve this issue for some time now and it has caused her great inconvenience and worry about the loss of such a large portion of her pension.

Putting things right

My aim is that Ms L should be put as closely as possible into the position she would probably now be in if she had been given suitable advice.

I take the view that Ms L would have invested differently. It's not possible to say precisely what she would have done differently. But I'm satisfied that what I've set out below is fair and reasonable given Ms L's circumstances and objectives when she invested.

What must IUK do?

To compensate Ms L fairly, IUK must:

- Compare the performance of Ms L's investment with that of 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.
- IUK should also add any interest set out below to the compensation payable.
- IUK should pay into Ms L's pension plan to increase its value by the total amount of the compensation and any interest. The amount paid should allow for the effect of charges and any available tax relief. Compensation should not be paid into the pension plan if it would conflict with any existing protection or allowance.
- If IUK is unable to pay the total amount into Ms L's pension plan, it should pay that amount direct to her. But had it been possible to pay into the plan, it would have provided a taxable income. Therefore the total amount 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 Ms L won't be able to reclaim any of the reduction after compensation is paid.
- The notional allowance should be calculated using Ms L's actual or expected marginal rate of tax at her selected retirement age.
- It's reasonable to assume that Ms L is likely to be a basic rate taxpayer at the selected retirement age, so the reduction would equal 20%. However, if Ms L would have been able to take a tax free lump sum, the reduction should be applied to 75% of the compensation, resulting in an overall reduction of 15%.
- In addition IUK must also pay directly to Ms L a sum of £300 for the worry and time taken in resolving this issue.

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

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Momentum SIPP	Some liquid/some illiquid	FTSE UK Private Investors Income Total Return Index	Date of investment	Date of my final decision	8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance)

Actual value

This means the actual amount of Ms L's pension at the end date.

It may be difficult to find the *actual* value of the portfolio. This is complicated where an asset is illiquid (meaning it could not be readily sold on the open market) as in this case. IUK should take ownership of any illiquid assets by paying a commercial value acceptable to the pension provider. The amount IUK pays should be included in the actual value before compensation is calculated.

If IUK is unable to purchase illiquid assets, their value should be assumed to be nil for the purpose of calculating the actual value. IUK may require that Ms L provides an undertaking to pay IUK any amount she may receive from the illiquid assets in the future. That undertaking must allow for any tax and charges that would be incurred on drawing the receipt from the pension plan. IUK will need to meet any costs in drawing up the undertaking.

Fair value

This is what the pension fund 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 Momentum 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 IUK totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically.

The Momentum SIPP only exists because of illiquid assets. In order for the Momentum SIPP to be closed and further fees that are charged to be prevented, those investments need to

be removed. I've set out above how this might be achieved by IUK taking over the portfolio, or this is something that Ms L can discuss with the provider directly. But I don't know how long that will take.

Third parties are involved and we don't have the power to tell them what to do. If you are unable to purchase the portfolio, to provide certainty to all parties I think it's fair that you pay Ms L an upfront lump sum equivalent to five years' worth of wrapper fees (calculated using the fee in the previous year to date). This should provide a reasonable period for the parties to arrange for the Momentum SIPP to be closed.

Why is this remedy suitable?

I've decided on this method of compensation because:

- Ms L 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 would be 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 Ms L's circumstances and risk attitude.

My final decision

I uphold the complaint. My decision is that Inter-UK Financial Services Limited should pay the amount calculated as set out above.

Inter-UK Financial Services Limited should provide details of its calculation to Ms L in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms L to accept or reject my decision before 17 August 2023.

Martin Catherwood
Ombudsman