DRN-4428467

The complaint

The estate of Mrs S complains about the way KW Wealth Planning Limited trading as Kingswood Group managed the late Mrs S's portfolio. It says some of the investments were unsuitable and these caused a financial loss.

What happened

In 2014 Mrs S transferred her existing discretionary portfolio to KWPL. As part of its onboarding process, Mrs S filled out an investment questionnaire with KWPL which set out some key information about her and her financial circumstances. This document showed that she was earning over £110,000 in income from various sources, was spending around £16,000 a year and had around £192,000 in cash savings. The questionnaire also said that she had around £1.6million in stocks and shares, £234,000 in bonds and £15,000 in national savings. At the time, her attitude to risk was identified as 'lower/medium risk'. This involved a 50% fixed interest and equity split with Ms S's objective being to provide for her day to day needs and protecting her capital against inflation.

In 2016 Mrs S updated her investment profile with KWPL. The profile set out some additional key information about her, including her knowledge, experience and overall financial circumstances. In summary:

- She had knowledge of a range of investments, including bonds, savings, investment bonds, unit trusts and OEICs, ETFs, investment trusts, shares and UCIS. She had no knowledge of complex pension arrangements, derivatives, VCT, EIS or BPRA schemes or guaranteed investments. She confirmed that she had previously invested in UCIS.
- She held around £240,000 in cash and was expecting her portfolio to be around £1.6million. She was looking to achieve her goals within two to five years, and whilst she was looking for income primarily, this was 'not as important as it was'.
- In terms of risk she answered five questions. Broadly speaking, she accepted that her portfolio would be exposed to some risk and that it would fluctuate in value in order to maximise her potential for long term growth. However, she would not feel comfortable with a loss of 20%.
- Her attitude to investment showed that she would be unlikely to spend any of the invested capital and that she wanted steady and predictable returns, rather than 'dramatic swings' in value.
- Her capacity for loss showed that she could maintain a loss of up to 19% of her portfolio.
- The total of these scores put her in KWPL's 'Category 3':

'50% fixed income and 50% equity investment: This strategy is expected to deliver a balance between longer term capital growth and income with medium risk. In order to achieve this, the strategy is mostly invested in equities and fixed income instruments'.

The notes also gave a bit more context about the late Mrs S's objectives. They said that the portfolio was set up when her husband was alive and it provided an income to allow them to travel and for his private health care. The notes explained that while Mrs S travelled less after his passing, she liked seeing her bank balance grow knowing she could call on it at any time. As the balance had grown by around £50,000 in two years, the advisers noted that this income was likely surplus but was something Mrs S was keen on. He noted that her other objective was otherwise 'to invest to preserve capital from inflation impact to retain its real value'.

Between 2014 and June 2018 KWPL managed the portfolio on a discretionary basis. During this time Mrs S's portfolio had a broad equity and 'non-equity' split. Crucially, within what KWPL claimed was the 'lower risk' part of the portfolio, it had purchased on her behalf units in two Unregulated Collective Investments (UCIS):

- Prestige Alternative Finance (Prestige); this UCIS focused on investing in 'asset-based direct lending'. Between 2015 and 2018 KWPL invested £215,000 in this fund.

- TCA Global Credit Master Fund (TCA); this UCIS focused on investing in 'short term, senior secure, direct lending and advisory services for small and medium enterprises'. Typically the fund invested primarily in the USA, with some exposure to EU/UK, Canada and New Zealand. Between 2014 and 2018, KWPL invested £208,000 in this fund.

During the period in question, the combined total of these investments amounted to about 25% of Mrs S's portfolio – this was in part also due to increases in the values of both funds. In June 2018 the arrangement changed as a result of Mrs S's power of attorney's (POAs) involvement. The portfolio then became an advisory one until it was transferred to another firm.

In March 2021 Mrs S's POAs complained to KWPL. In short they complained that as a result of a fraud allegation in the management of the TCA UCIS, the portfolio stood to lose the entire investment. And they said that neither UCIS's were suitable for Mrs S and the proportion invested was far too much. KWPL looked into their complaint but didn't agree it had done anything wrong. It said that both investments were suitable for Mrs S as a high net worth investor, and that the Prestige UCIS made a gain of around 25% when it was sold. It said that the only reason the TCA UCIS was making such a significant loss was due to it being in liquidation as a result of fraud, and this was not something KWPL was responsible for or could foresee.

Shortly after this, Mrs S sadly passed away. The executors of her estate referred the complaint to this service. One of our investigators looked into the complaint and concluded it should be upheld. In short, he considered that UCIS were not suitable investments for Mrs S given her attitude to risk, age and investment objectives. He recommended both TCA and Prestige be compared to a benchmark, and any difference in return refunded to the estate.

The late Mrs S's estate agreed, but KWPL did not. It made detailed comments in response:

- Mrs S was not averse to risk and the answers she gave in her investment profile demonstrated this. She was prepared to accept some investment risk to achieve her investment goals – and had indicated she was comfortable with losses up to 19%.
- The investments in TCA and Prestige 'were part of a diverse range of investments taken out and maintained as part of Mrs S's investment portfolio as a whole'. This was part of a balance of fixed income and equities.

- The advisor had the balance of the portfolio 'uppermost' in mind when considering investment decisions. He explained in 2020 that 'by removing TCA and Prestige from the portfolio, it skews the asset allocation towards equities and in theory to higher risk assets'. He concluded that such a disposal would essentially make the portfolio 75% equities and 25% non-equities.

- KWPL said this showed that the portfolio overall 'was not particularly high risk and was appropriate' for Mrs S. It said the evidence showed the adviser was conscious of this 'and concerned about the imbalance of holding too many equity based investments'.

- It said that the advisor could not have known about the fraud issues within the TCA fund, and it would be unfair to penalise the advisor for recommending that investment with the benefit of hindsight.

- It said that it noted the investigator's conclusions about the allocation of 25% of the portfolio to UCIS, but it said that the return made on the sale of Prestige compared to the returns on other fixed income demonstrated that it was the right call to make. It reiterated it's argument that it was unfair to only look at one part of the portfolio, and all of the portfolio should be taken into account.

- It said that whilst the investigator had pointed out other investments which KWPL could've bought on Mrs S's behalf, its view at the time was that gilts were considered to be 'one of the most risky'. It said this was evidenced in 2022 when gilt markets fell by 23%. It said that the portfolio was finely balanced. And it said that the advisor's opinion of both UCIS was that they were less volatile than other investments and had delivered consistent returns.

- It disagreed with the investigator that Mrs S wouldn't have understood the risks of Prestige and TCA, and said she had signed a high net worth letter which set out some risks, and her experience supported its understanding. It said that she had previously invested into two other UCIS. It said that the service shouldn't overstate Mrs S's age and vulnerabilities at the time, as she was an experienced investor who had held the portfolio for many years and was fully informed of the risks. It disagreed with the investigator's method for awarding compensation, and argued that a gilt index would be more appropriate.

- It said that any calculation ought to stop at the point at which the POAs were appointed in 2014 or at the latest when the arrangement with KWPL became advisory. It said that they had agreed to sign, in 2018, another high net worth statement which specifically alerted them to the risk that 'the investments to which the promotions will relate may expose me to a significant risk of losing all of the money or other property invested'. It also said that in 2019, when the POAs were in the process of transferring the portfolio to another firm, it had said it was unable to hold the two UCIS. Therefore, the POAs were on notice at the time about problems with these assets – and could've sold them then if they wanted to. Had they done this, the TCA fund would've had a value that could've been realised, thereby avoiding the substantial loss now incurred.

In October 2023, I issued a provisional decision. In it I said:

Whilst I've considered KWPL's comments very carefully, I'm not persuaded it has clearly explained why this non-equity portion of the portfolio was suitable for a medium low risk investor like Mrs S – particularly in view of the limited requirements from the portfolio, her modest expenditure and crucially her attitude to investment risk.

KWPL has made the argument that the losses on the TCA UCIS were not foreseeable, and that Prestige turned a profit – when the gilt market had dropped. But to my mind, these are performance considerations which I don't agree are relevant to establishing the suitability of these investments for Mrs S. Whilst I've not reviewed what due diligence KWPL carried out on TCA, it's clear to me that it had no ability to know in advance how an investment would perform. I'm also persuaded by the evidence I've seen that KWPL legitimately believed these investments were worthwhile, and would make a return in the future.

I also agree with KWPL that it isn't fair to look at the two UCIS in isolation. It's clear to me that the advisor was keen on ensuring an adequate balance in the portfolio and believed that both these UCIS counteracted the equity or higher risk portion of the portfolio. And I'm satisfied that given everything that was known about Mrs S at the time, it wasn't inherently unsuitable to invest in some UCIS on her behalf. What I mean here is that given everything that KWPL knew about Mrs S, the question isn't the suitability of UCIS per se.

What I've considered is to what extent these investments made her whole portfolio unsuitable. And it's the effect of these two investments on her overall portfolio that in my view means I should uphold the executor's complaint.

I say this firstly because I don't agree that considering these investments as 'lower risk' was fair and reasonable. I think the FCA has been clear that these investments are not 'lower risk', and are not going to be suitable for the majority of consumers. Furthermore, whilst Mrs S was high net worth, it did not automatically follow that she should be significantly exposed to the inherent risks that these types of investments represent. As I've said above, I can understand why consideration was given to alternative investments in the context of Mrs S's varied and large portfolio – but to have at various points in time a quarter of her portfolio invested in UCIS in my view unfairly disregarded her attitude to risk and her objectives.

Furthermore, KWPL has attempted to argue both in response to the complaint and at the time, that removing these UCIS from the portfolio would have skewed the risk of the portfolio towards the higher end because it would've resulted in it having around 70% in equities. In my view, this shows that the portfolio was therefore not aligned with the amount of risk that Mrs S was willing to take with her money. This was not a justification for keeping these investments in the portfolio – in my view the level of equities in her portfolio was the very reason why Mrs S should not have had such a large proportion of the remainder invested in UCIS.

In my view, the very fact that removing both these UCIS meant that the portfolio would be 70% invested in equities shows that the portfolio was in fact not medium lower risk as Mrs S wanted – it was clearly carrying a much higher level of risk that she wanted or had indicated she was comfortable with.

The reality is that both these unregulated investments were not low risk. And whilst they may well have outperformed other mainstream investments, such as gilts, I'm satisfied that given the FCA's guidance which I've quoted above, it wasn't fair and reasonable for the adviser to have concluded that these investments would counteract the equity portion of the portfolio.

In my view, both these investments needed to be properly considered within the equity portion of Mrs S's portfolio in order for KWPL to ensure that Mrs S's portfolio remained aligned to her objectives and attitude to risk.

As a result, I agree with the investigator that Mrs S's portfolio was unsuitable for her, and I consider that KWPL needs to put things right. However, I've disagreed with how this should be done, and explain why below.

In putting things right for the estate of Mrs S, my objective is to put it in the position it would've been had Mrs S been suitably advised and her portfolio been suitably managed. As I've outlined above, I'm satisfied that the UCIS which KWPL bought on her behalf made the portfolio unsuitable – but I'm also satisfied that the adviser did have the whole portfolio in mind when investing in them.

As I've also said, the investments themselves were not inherently unsuitable for Mrs S – but it's the amount of her portfolio that was exposed to them, combined with the level of other equities she was invested in, which made the resulting portfolio unsuitable for her. It's important I note this, because it goes to the heart of what KWPL should do to put things right. It's clear to me that in essentially only compensating for these two investments, I wouldn't be putting the estate of Mrs S back in the position it would've been had the late Mrs S's portfolio been suitably managed.

I say this because in my view, the rest of the portfolio would've looked different had KWPL not invested in these two UCIS. I can't say precisely how it would've looked different, or what other strategies it may have employed in order to reduce the risk of the portfolio overall. So it is not possible to say precisely what the late Mrs S would have done. But I am satisfied that what I have set out below is fair and reasonable given Mrs S' circumstances and objectives when she invested.

I also have to be mindful of removing or avoiding any benefit of hindsight when putting matters right. The adviser didn't know in advance how investments would perform. What all this means is that I think taking out these two investments from the portfolio, and disregarding how the remainder of the portfolio performed, is not fair and reasonable. I'm satisfied that as Mrs S's portfolio was being managed holistically, and since I've concluded that these investments made the whole portfolio unsuitable, it's fair and reasonable that the benchmark ought to take into account the portfolio's performance overall, including these two investments.

Finally, KWPL has also argued that the end date ought to be when the arrangement ceased to be discretionary. I've considered this argument but I don't currently agree that's fair. Whilst it's clear that the late Mrs S's POAs were on notice about these UCIS, I've seen no evidence that KWPL at any point advised them to sell these investments. In fact, I've seen the opposite – that is KWPL explaining why these two investments shouldn't be sold, because of the impact on the rest of the portfolio. Therefore I'm satisfied that the end date ought to be the date the portfolio was transferred.

I recommended that KWPL compare the performance of the portfolio with a benchmark to determine the loss to the estate.

The estate of Mrs S agreed with my provisional decision, but KWPL did not. It provided detailed comments in response. It said:

- The relative exposure to UCIS in Mrs S's portfolio was constantly diminishing by virtue of her income surplus.

- It disputed that around 25% of the portfolio was invested in UCIS, and noted that this was in fact around 17.7%.

- It said that by investing in UCIS at different times, there was greater protection to Mrs S's investment in the form of pound cost averaging. It reiterated that the loss suffered on the investment was due to fraud which was not something KWPL was responsible for.

- Mrs S did not rely on the investments and the investments in UCIS 'provided a greater element of diversification within the client's holistic portfolio and reduced risk overall'.

- It also reiterated that given Mrs S's significant income surplus, the concentration of Mrs S's investments into the UCIS would drop significantly over the years – and it gave examples of how that would happen dropping by over 2% by 2021.

- It referred to a case study on this service's website and noted parallels between the two cases, including the fact that Mrs S was a high net worth individual.

- It said that Mrs S power of attorneys failed to act in her best interests by not raising any concerns about the UCIS investments prior to 2021. In summary, KWPL said that the POAs could've raised concerns about the UCIS earlier than 2021, and in particular in 2019 when another firm would've accepted the investments. At that point they could've been liquidated but weren't.

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.

For completeness, I've set out the relevant regulatory background, as I did in my provisional decision, here.

There were rules which governed how KWPL needed to manage the late Mrs S's portfolio, and for ease of reference I set these out below.

Applicable standards and guidance

In 2014, the Financial Conduct Authority's rules for businesses advising on investments were set out in COBS 9 – Suitability. Whilst the provisions changed a little between 2014 and 2018, I've only set out the wording of the rules in 2014 as I consider the changes minor and did not fundamentally alter KWPL's obligations with respect to Mrs S's portfolio.

Assessing suitability: the obligations

COBS 9.2.1 R 01/11/2007 RP

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

(2) When making the personal recommendation or managing his investments, the firm must obtain the necessary information regarding the client's:
    a. knowledge and experience in the investment field relevant to the specific type of designated investment or service;
    b. financial situation; and
    c. investment objectives;

so as to enable the firm to make the recommendation, or take the decision, which is suitable for him.

COBS 9.2.2 R 01/11/2007 RP

(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.

(2) The information regarding the investment objectives of a client must include, where relevant, information on the length of time for which he wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.

(3) The information regarding the financial situation of a client must include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.

COBS 9.2.3 R 01/11/2007 RP

The information regarding a client's knowledge and experience in the investment field includes, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved, information on:

(1) the types of service, transaction and designated investment with which the client is familiar;
(2) the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;
(3) the level of education, profession or relevant former profession of the client.

The FCA has over the course of the period in question also provided its own view on UCIS. It, and its predecessor the FSA, has consistently said that UCIS are 'high risk investments' due to their often illiquid nature and unregulated status, which allows UCIS fund managers to invest in 'riskier assets or use riskier investment strategies than authorised or recognised schemes'. It warns consumers that UCIS 'is considered a high risk investment and you should be prepared to lose all your money'.

My findings in light of KWPL's comments

I've carefully considered the comments that KWP has provided. However, I'm not persuaded to change my provisional findings, and I therefore confirm them as final.

KWPL has made references to Mrs S's income surplus and its effect on the concentration of Mrs S's portfolio in the two UCIS.

It has also said that the concentration of Mrs S's portfolio wasn't as much as 25% in the two UCIS.

I accept the relative proportion fluctuated, but by July 2018 KWPL confirmed to her POAs that her total exposure was over 25%, at 27.66% - this was 'a little over half her low risk element'. The key part, the letter said, was that these UCIS were 'risk reducers'.

Furthermore, whilst I accept that investments in TCA and Prestige were made with a view to the whole portfolio, I don't agree that all of Mrs S's net worth was taken into account. For example, her review in 2014 clearly makes reference to the £1.6m from the sale of the business, and specifically relates to the portfolio only. Whilst her overall financial circumstances were taken into account in establishing the relevant risk tolerance (and, for example, whether she needed additional cash within the portfolio), it's the percentage of UCIS in the portfolio that's relevant to whether it was aligned with her attitude to risk.

In any event, even if I accepted KWPL's arguments (and for the reasons I've set out above, I'm not persuaded), including that Mrs S's portfolio wasn't *always* as exposed to the two UCIS, I consider that almost 18% of Mrs S's portfolio invested in UCIS would still have been unsuitable for her – and for the same reasons I already gave in my provisional decision. It's clear to me that this element of her portfolio was seen as 'lower risk', and for the reasons I gave in my provisional decision (and which I confirm here as final) this wasn't fair and reasonable. In my view, given the rest of the portfolio was weighted significantly in equities, it wasn't fair and reasonable for KWPL to conclude that it was suitable to invest so much of Mrs S's portfolio in UCIS.

And I'm not persuaded it's fair that I consider Mrs S's bank balance and how much it was growing or would've grown but for her passing. In my view, Mrs S was clear that her bank balance was something separate to her portfolio and how it was being managed, and I've seen no evidence that in determining the risk of Mrs S's portfolio, or the trading decisions it was making on her behalf, KWPL included her bank balance as part of its valuations.

Finally, I'm not persuaded I have sufficient evidence to conclude that the POAs are in some way responsible for not selling or liquidating these investments sooner. It's clear to me that they were reliant on KWPL as their advisers, and for the reasons I've already given in my provisional decision, its advice was clearly against selling these investments – nor did it ever allude to the investments potentially being too high risk or unsuitable. So I remain of the view that the end date for any calculation of compensation ought to be when the portfolio was moved to the new adviser.

In relation to the case study, whilst I understand why KWPL has raised it, I think it illustrates the approach I've taken here. The issue isn't just about Mrs S being high net worth – in order to establish whether KWPL treated her fairly, I've taken into account her attitude to risk (which was never recorded as high), her objectives for the portfolio as well as the proportion of her portfolio that was invested in UCIS. It's all of these factors combined that have led me to conclude, in my provisional decision and in this final decision, that it wasn't fair and reasonable for KWPL to have invested Mrs S's portfolio the way that it did.

So for the reasons I've given, I'm satisfied the estate of Mrs S's complaint should be upheld and compensation is payable. As I've had no comments on my approach to putting things right, I see no reason to depart from my provisional conclusions and I therefore set them out again below.

Putting things right

In assessing what would be fair compensation, I consider that my aim should be to put the estate of Mrs S as close to the position it would probably now be in if Mrs S's portfolio had been suitable for her. I take the view that Mrs S's portfolio would've been invested differently. It is not possible to say *precisely* what Mrs S would've been invested in. But I am satisfied that what I have set out below is fair and reasonable given Mrs S's circumstances and objectives when she invested.

What must KWPL do?

To compensate the estate of Mrs S fairly, KWPL must:

- Compare the performance of Mrs S' investment with that of the benchmark shown below and pay the difference between the *fair value* and the *actual value* of the investments. If the *actual value* is greater than the *fair value*, no compensation is payable.

- KWPL should also add any interest set out below to the compensation payable.

Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
The portfolio	No longer in force	FTSE UK Private Investors Income Total Return Index	Date of investment	Date ceased to be held	8% simple per year on any loss from the end date to the date of settlement

Actual value

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

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 portfolio 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 KWPL totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically.

I understand the TCA UCIS is currently illiquid. KWPL will need to take ownership of that investment, and assume its value is £0 for the purposes of the calculation above. If KWPL cannot take ownership of the investment, then the estate of Mrs S will need to provide an undertaking that any future payments out of this fund will be paid back to KWPL in future.

Why is this remedy suitable?

I have decided on this method of compensation because:

- Mrs S 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 a mix of diversified indices representing 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 Mrs S' circumstances and risk attitude.

My final decision

Where I uphold a complaint, I can make a money award requiring a financial business to pay compensation of up to £160,000, plus any interest and/or costs that I consider appropriate. If I consider that fair compensation exceeds £160,000, I may recommend the business to pay the balance.

KW Wealth Planning Limited trading as Kingswood Group should provide details of its calculation to the estate of Mrs S in a clear, simple format.

Recommendation: If the amount produced by the calculation of fair compensation exceeds £160,000, I recommend that KW Wealth Planning Limited trading as Kingswood Group pays the estate of Mrs S the balance plus any interest on that amount as set out above.

This recommendation is not part of my determination or award. It does not bind KW Wealth Planning Limited trading as Kingswood Group. It is unlikely that the estate of Mrs S can accept my decision and go to court to ask for the balance. The estate of Mrs S may want to consider getting independent legal advice before deciding whether to accept this decision.

Determination and award: I uphold the complaint. I consider that fair compensation should be calculated as set out above. My decision is that KW Wealth Planning Limited trading as Kingswood Group should pay the estate of Mrs S the amount produced by that calculation – up to a maximum of £160,000 plus any interest set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask the estate of Mrs S to accept or reject my decision before 12 December 2023.

Alessandro Pulzone
Ombudsman