DRN-4663896

The complaint

Mr N has complained about the way that Hargreaves Lansdown Asset Management Limited ('HL') promoted an investment he purchased.

What happened

The investment Mr N bought from HL was called the Woodford Equity Income Fund ('WEIF') and was managed by Neil Woodford, who left Invesco Perpetual in 2013 to set up Woodford Investment Management ('WIM'). The WEIF was launched in May 2014 with a £1 per unit fixed offer price until 18 June 2014. The Authorised Corporate Director (ACD) of the fund was Capita Financial Managers, later known as Link Fund Solutions.

The WEIF broadly tracked the benchmarks (albeit whilst providing a greater return and experiencing some more volatility) until the second half of 2017, when there was a significant fall which was not experienced by the benchmarks. It began to significantly underperform benchmarks from early 2018 and the performance followed a very different pattern to the benchmarks from early 2019 to the date of suspension.

Alongside this, the fund began to see significant outflows from mid-2017, falling from around £10bn of assets under management to around £3bn in two years.

In June 2019 the extent of those outflows - and the portion of the WEIF's assets which were not liquid - led Link to decide to suspend trading in the fund. Link removed WIM as the investment manager around this time.

The fund did not trade again. Later in 2019, Link decided to liquidate the fund. Investors have since received payments as and when the fund's assets have been sold. A small amount remains invested in assets which are not liquid i.e. cannot currently be sold. A scheme of arrangement between investors and Link has now been sanctioned by the court and will conclude the wind up of the fund with further distributions being made to investors who held units in the fund at suspension.

HL's communications relating to the WEIF

HL's relationship with WIM and the WEIF began prior to the fund's launch. HL met with WIM in early 2014 and decided to promote the WEIF to its customers and visitors to its website ahead of the fund's launch.

The WEIF was the subject of, or featured in, many communications from HL over the period from the fund's launch to its suspension. HL's communications relating to the WEIF can be categorised broadly as follows:

- Promotion of the WEIF at its launch by letter and through website articles and emails.
- Ongoing promotion of the WEIF through website articles (and, in some instances, emails alerting the recipient to the article).
- Updates on the WEIF through website articles (and emails alerting the recipient to the article).

- The inclusion of the WEIF in "best buy" lists – called the Wealth 150 (which had a subset of discounted funds called the Wealth 150+) and, later, the Wealth 50 – both of which were shared on its website, through emails and via Wealth Reports, which were included in the Investment Times sent to its clients by post.

The Wealth List

HL published a list of what it considered, in its view, to be the "best" or "favourite" funds. This was initially called the Wealth 150 (and a subset of this, featuring discounted management charges for HL clients, the Wealth 150+) then later the Wealth 50 – I'll refer to these generally as the Wealth Lists. The WEIF featured on the Wealth List from its launch until its suspension.

I understand the list was available on HL's website to any visitor and also sent to all customers on its general mailing list who had elected to receive communications, alongside the bi-annual Wealth Reports published by HL. HL says the list was updated from time-to-time with funds being added or removed as a result of the ongoing cycle of review, monitoring and analysis of funds by its investment team.

As part of its ongoing research HL met with WIM to discuss the WEIF on a number of occasions.

Mr N's dealings in the WEIF

In April 2015 Mr N received advice from HL to transfer ISA funds into an HL Vantage ISA. HL recommended that 12.5% of these funds be invested in the WEIF. In June 2015 units in the WEIF costing £10,834.74 were purchased in Mr N's HL ISA.

In May 2016 HL advised Mr N to transfer funds from a group personal pension into an HL self-invested personal pension ('SIPP'). HL again recommended investment of 12.5% of the funds into the WEIF. This resulted in Mr N purchasing £16,453.17 of units in the WEIF in July 2016.

Mr N's complaint to HL and its response

In 2019, shortly after the suspension of the WEIF, Mr N made a complaint to HL. He commented about concerns he'd had regarding the HL adviser he met in 2015. He also questioned why the WEIF had initially been recommended as an investment for both his ISA and SIPP portfolios in 2015 and 2016.

I should clarify at this point that Mr N's concerns about the initial recommendations he received from HL to invest in the WEIF in 2015 and 2016 under his two portfolios, and his comments about the conduct of the 2015 adviser, have already been considered by this service in a separate complaint against HL's advisory arm. Those events therefore do not form part of the subject matter of the complaint I am considering here.

The elements of Mr N's 2019 complaint that I am considering in this decision relate to his concerns that the WEIF remained on HL's Wealth Lists from when he had invested in it until its suspension. Mr N said that HL had actively promoted the fund throughout the time that he held it. He suggested that HL's articles about the WEIF represented dishonest financial promotions, rather than a balanced commentary. As a result, Mr N said he felt he had been misled by HL.

Mr N commented that HL had had concerns about the composition of the WEIF as early as 2017, but continued to promote it and put a positive spin on it. He questioned the relationship between Woodford and HL, stating that the fund's performance declined whilst its holdings of riskier and illiquid assets rose. Mr N said that HL had disregarded the interests of its clients. He highlighted commentary provided by HL about the WEIF on 9 January 2018, 22 March 2018, 7 January 2019, 1 March 2019 and 5 June 2019. He said that whilst HL had met with Neil Woodford and his team on many occasions, concerns were never communicated to HL clients in an honest and transparent way.

Mr N suggested that HL had breached regulatory rules when presenting the WEIF in the way that it had. He said the suspension of the fund had caused him considerable distress in relation to his financial planning, and he asked HL to compensate him for his financial loss on the fund.

In response, whilst HL acknowledged the WEIF's "*difficult period of performance*" during 2018 and 2019, it said that its "*conviction in its long term prospects remained.*" It stated that it believed the WEIF had the potential to outperform its benchmark, and that is why it remained on HL's Wealth Lists. HL commented that after it had provided Mr N with the initial advice to invest in the WEIF, it had provided an 'execution only' service, meaning that it was not providing investment advice or making personal recommendations. That meant that it was up to Mr N whether to remain invested in any fund. HL said that it provided information compiled by its investment research team so that clients could decide where to invest. It stated that it had always made it clear that the WEIF came with risks and that there were no guarantees when investing.

Unhappy with HL's response, Mr N brought a complaint to this service.

Our investigator did not uphold this complaint. In summary he concluded that HL was free to take the view that it did about whether the WEIF should appear on the Wealth Lists, and it had acted reasonably when reaching this view. The investigator stated that whilst HL had concerns about the fund, it continued to genuinely believe it should be on the Lists. He also said that HL had decided that a breach of the 10% limit on unquoted stocks would result in the WEIF being removed from the Wealth Lists but there was no evidence HL became aware of such a breach.

The investigator said that HL's communications had done enough to make Mr N aware of the increasing risk that came with the WEIF increasing its exposure to smaller companies. He highlighted that HL was not providing customers with a personal recommendation to invest, but was expressing an opinion about whether the WEIF was a good investment opportunity for clients making their own decisions. The investigator said that HL had provided Mr N with sufficient information to make his decision about whether to retain his existing investments in the WEIF. His view was that HL had acted fairly and reasonably in its dealings with Mr N.

Mr N explained how disappointed he was with the investigator's findings. He said that as its customer, HL had not put him first or treated him fairly. He also said HL had not acted honestly or professionally in his best interests as its client. Mr N suggested that HL had not ensured that its communications and financial promotions were clear, fair and not misleading.

Mr N commented that a claims management company was seeking to file a group action in the courts against HL relating to its continuing promotion of the WEIF up to its collapse, which he said was despite HL knowing about liquidity and diversification problems with the fund. He said he was not alone in terms of his grievance against HL and he referred to the number of HL clients who had raised similar experiences to his own. In light of this, Mr N questioned how all of these clients of HL could be wrong. In asking for his complaint to be passed to an ombudsman, Mr N suggested that a final decision should be delayed until the outcome of the group legal action he had referred to was determined.

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.

Firstly I note what Mr N has said about delaying a final decision being issued on this case until the group action he has referenced has been concluded. Whilst I acknowledge what Mr N has said, having carefully considered his comments my view is that it is reasonable for me to issue a decision at this time, based on the evidence available.

Mr N has described the level of upset he has been caused as a result of the financial loss he has experienced on his investments in the WEIF. I appreciate why this is the case, but on balance I'm not persuaded that HL's communications about the fund were misleading, or that HL should be liable for the losses that Mr N suffered.

I've first set out what I consider were the relevant regulatory obligations that HL's communications needed to meet.

What are the relevant regulatory obligations?

I think the following regulatory requirements are of particular relevance to my assessment of whether HL acted fairly and reasonably in its dealings in this case.

The Principles for Businesses, which are set out in the FCA's handbook "*are a general statement of the fundamental obligations of firms…under the regulatory system*" (PRIN 1.1.2G). I consider that Principles 6 and 7 are of particular relevance to this complaint. They say:

- Principle 6 – Customers' interests – "*A firm must pay due regard to the interests of its customers and treat them fairly.*"
- Principle 7 - Communications with clients – "*A firm must 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.*"

I have also taken into account the FCA rules for firms carrying on investment related business set out in the Conduct of Business Sourcebook (COBS). In particular, COBS 4.2.1R sets out the requirements on authorised firms, like HL, when communicating with clients. COBS 4.2.1R(1) says:

"*A firm must ensure that a communication or a financial promotion is fair, clear and not misleading.*"

COBS 2.1.1R (1) is also relevant to this complaint. It says:

"*A firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule).*"

My findings

At outset I should say that I appreciate Mr N's decision to retain his investments in the WEIF was influenced by HL's inclusion of the fund on its Wealth Lists. Mr N took into account what HL said about the WEIF, including its comments on the fund's long-term prospects.

But the rules (set out above) that HL was required to adhere to when making these communications required it to issue communications which were clear, fair and not misleading. This means that as long as HL's communications during the relevant period were factual and gave a balanced view of its assessment of the WEIF, then it didn't do anything wrong.

It's clear that HL provided significant positive commentary about Woodford and the WEIF prior to Mr N's investments in 2015 and 2016. HL obviously believed that Woodford's track record, as well as the objective and performance of the WEIF between 2014 and 2016, were such that it continued to be a fund that it thought met its criteria for inclusion on its Wealth Lists.

The evidence I've seen shows that whilst HL met numerous times between 2014 and 2016 with Woodford and had frank conversations about his management of the fund, its views were largely consistent with what it was telling its customers.

In December 2016, HL said on its website that the WEIF was "*not a typical equity income fund"* and said that unlike most equity income funds which were exposed to large high-yielding companies, "*only around 50%"* of the WEIF was invested in this area. The remainder was "*invested in small and medium sized companies, or those not listed on the stock market"*.

Based on the evidence provided, I think it's fair to say that Mr N ought to have known that the WEIF had certain risks associated with its investment strategy.

HL was explicit that the fund had *a "significant bias to smaller companies relative to the FTSE All Share Index which adds risk, and also has more invested in medium sized companies than the index"*. Ultimately HL's view was that this approach would "*add significant value for investors able to withstand the additional risk and volatility that comes from investing in smaller and unquoted companies."*

Having reviewed the evidence of HL's meetings with WIM in 2016, I can see that in summary it was aware that the WEIF was no longer a typical equity income fund. I can also see that it knew there had been a shift towards small cap and growth stocks which it had not expected – and it recognised that in the event of significant outflows, that proportion would increase and potentially affect WIM's ability to invest further. HL was also aware that its customers might not know how the fund had changed – and it agreed to take steps to address this. It's clear to me that the update above was designed to draw these concerns to their customer's attention.

But HL also continued to hold the view that the WEIF was still an investment that would add value for investors – and I'm satisfied it held that view internally and so it was clear, fair and not misleading to have continued to say that in its updates. It was for individual investors to decide for themselves whether the risks and the features of the WEIF which HL was describing were right for them.

I acknowledge that in 2017 the WEIF began to underperform its benchmark, but I'm satisfied that HL's continuing communications about the fund remained balanced. It was clear that it viewed the WEIF as a long term investment and explained in its June 2017 update that Woodford had "*a long history of making big stock or sector bets, and while these decisions have at times taken time to come to fruition, they have added significant value for investors over the long term"*.

In an article it published in September 2017 on its website, it explained that "*judging a fund manager over a time period of a few months is folly, especially one with such a long and* *distinguished track record"*. This article explained that Woodford had experienced poor performance in the past, and that it was *"quite right to question any fund manager on their performance",* which HL said it had done. But it explained that his approach involved seeking out undervalued companies and this strategy had "*seen his investors well-rewarded over the long term"*.

In its November 2017 Wealth Report HL said that performance "*over the past year has been disappointing relative to the FTSE All Share Index"* and that some of Woodford's stock selections had under-performed. But HL continued to have "*faith in his abilities to deliver for investors".* In my view HL was entitled to continue to believe in the long term prospects of the WEIF – and I'm not persuaded it was misleading for it to communicate its view that, over the long term, the WEIF would still be a good investment. I'm also not persuaded that this belief, and its communication of it, was inconsistent with the obligations I've set out above.

In December 2017 HL said on its website that the WEIF wasn't "*a typical equity income fund"* and highlighted that around 9.5% of the fund was in unquoted companies. HL explained clearly that "*small and unquoted businesses are typically considered higher-risk because their shares are difficult to sell"*. And it concluded that Woodford's approach would "*result in periods of poor performance"* but it was "*premature to write Neil Woodford off"*.

The key issue here is that none of these updates differed markedly from the concerns HL was expressing to Woodford throughout the year and from its internally held view that whilst the fund was suffering from a period of poor performance, over the long term the investment would come good. The evidence shows that HL was aware of the WEIF nearing the 10% limit and was clearly aware of the poor performance of the fund.

I've seen evidence that it robustly challenged WIM when necessary, but it was also reassured by WIM's responses to those concerns – in particular in relation to the levels of unquoted stock. Ultimately, HL continued to believe that periods of poor performance were temporary, and that whilst it was important to ensure it was open about the nature of the WEIF and how it had changed, it continued to believe it was a good investment for the long term.

It's clear to me that Mr N had sufficient information from these updates to know that the WEIF was not a typical equity investment, and that there were specific risks in the way the WEIF was managed that he needed to be comfortable with.

In that context, I don't agree that the message that HL continued to believe the fund would improve its performance in the long term was misleading, because HL believed that to be the case – and was entitled to that reasonably held belief.

And I'm satisfied that HL's communications in 2018 and 2019 were equally clear, fair and not misleading. Mr N has referred to several communications issued by HL during this period that he has described as misleading. The excerpt he has provided from 9 January 2018 includes some detail from HL's 19 December 2017 update, and stated "*we believe it's premature to write Neil Woodford off.*" HL continued by saying that Woodford's long term record was outstanding, and that it continued to believe he had the ability to add value for investors over the long run. In my view these comments were broadly consistent with the available evidence about HL's view of the WEIF. Overall HL's view was that it should continue to support the fund on the basis that it would come good over the longer term. I consider HL explained the reasons for that view in a clear and fair way.

Mr N has referred to HL's 22 March 2018 update. This followed WEIF's change of sector classification. It clearly explained how almost "*40% of the fund is invested in small and mid-sized lower-yielding companies"* with "*an additional 10% invested in companies not yet listed* *on the stock market"*. HL said that it accepted Woodford's approach would "*lead to tough periods of performance"* but that it remained "*comfortable with the inclusion of unquoted companies"* although it did not "*want to see them increase as a proportion of the fund from here"*. It reminded investors to "*ensure they are comfortable with the investment approach and risks"*.

The evidence I've seen of HL's internal views and the meetings it had with WIM during 2018 show that HL was largely reassured that WIM had taken onboard its feedback, particularly in relation to continued investment in unquoted stock. And this is clearly reflected in the communication above. Internally it continued to believe that the fund would come good in the long term, but it acknowledged that it needed to ensure clients were aware of the nature of the fund, the need to diversify and the strategy WIM was following. In my view, the updates I've quoted above achieve this in a clear, fair and not misleading way.

Mr N has referenced comments made in HL's update on 7 January 2019. This explained its recent catch-up with Woodford. It said that although it had been a long-term supporter of Woodford, "*his funds have recently performed poorly"* and so it had been "*an uncomfortable time to hold the fund and our own conviction has been tested"*. The update then went on to explain why HL continued to keep the fund on its Wealth 50 and provided a detailed explanation of how the WEIF had changed since its launch, and some of the inherent risks of Woodford's approach to investing. It said it was clear that some of Woodford's investments hadn't "*paid off"*, and importantly highlighted to investors "*the importance of having a diversified portfolio, spreading your investments amongst managers that invest differently"*.

It concluded by saying that it was "*understandable that some investors are getting impatient with Woodford"* and that it had also "*been disappointed with recent performance"*. But it said that its approach was to back proven managers for the long-term and "*as part of a diversified portfolio, we still think Woodford has a place".*

Crucially, it said:

"*We could be wrong. If we are we'll put our hands up. It might be tempting to change our opinion now to be rid of the current discomfort, but we don't think it would be the right thing to do"*.

Mr N has highlighted comments made in HL's update on 1 March 2019, where it explained about the transfer of unlisted investments in the WEIF, describing it as a "*positive step*". Further updates highlighted that Woodford was experiencing "*his worst spell of performance"* and the fact that HL had been urging Woodford to *"address the weighting* [of unquoted] *stocks in his portfolio". O*verall it said that Woodford had "*shown an ability to make the big calls right, and when he does, investors profit"*.

Mr N has also included excerpts from an update on 5 June 2019. This confirmed performance achieved by Woodford over the last 10 years, and explained how HL chose funds for its Wealth Lists.

During this period, the evidence shows that HL was in regular contact with Woodford in a bid to understand the challenges he was facing in managing the fund and to ensure that its faith in his ability to turn things around wasn't mis-placed. The suspension of three stocks on the Guernsey exchange was a significant cause for concern – but this suspension was only temporary.

Furthermore, although it discussed whether the time had now come to remove the WEIF from its Wealth List, it's clear that internally it also considered the likelihood that the WEIF would recover. It had been reassured by WIM that it would deal with the level of unquoted stock in the portfolio – and HL told its clients this. I'm satisfied at this point, HL was clearly finding a way to balance communicating the risks and its concerns to consumers, while at the same time being open that it continued to believe that the WEIF would recover in the longer term.

When looking at the updates it provided, I think it's clear that HL was saying that there were risks in remaining invested in the WEIF, and that the performance had now been disappointing for some time. But it was entitled to tell its clients that it believed the fund would recover because that is what it believed internally at the time, for reasons which it gave in its updates.

Overall it's clear that there were periods between 2016 and 2019 when HL raised concerns with Woodford, for example around the level of unquoted stock in the WEIF, but it explained these concerns in its public updates or Wealth Lists. At the same time, it held the view that whilst there were some concerns in the short term, over the long term the WEIF would end up being a good investment for its clients. HL was entitled to hold that view, and I've seen insufficient evidence that it came to that conclusion unreasonably or in a way that was not genuinely based on its assessment of the WEIF and its future prospects.

Whilst I appreciate HL's view has turned out to be wrong, largely as a result of the liquidation of the fund which was not something it had anticipated, I don't consider that means its communications were not clear, fair and not misleading.

In my view HL clearly explained the risks of the fund, the areas where it had concerns and the reasons why it thought it was still worthwhile to hold it as part of a diversified portfolio. It was then for individual investors to decide for themselves whether holding the WEIF remained suitable for them, in light of HL's information, the risks as described, and the ongoing period of under-performance.

I am sorry to learn of the losses that Mr N suffered with his investments in the WEIF, and I appreciate my conclusions will be disappointing to him. But I'm satisfied that these losses were not caused by something HL did or didn't do, or because it misled Mr N in any way. I consider the losses were caused by the performance of the underlying investments in the WEIF, and its subsequent liquidation by the authorised corporate director.

My final decision

My final decision is that I do not uphold this complaint, and I make no award.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr N to accept or reject my decision before 14 November 2024.

John Swain
Ombudsman