DRN-4775670

The complaint

Ms L says the advice given by Applewood Independent Limited (AIL), to switch her three personal pensions into a Self-invested Personal Pension (SIPP) and higher risk investments was unsuitable.

What happened

Ms L contacted AIL to review her financial circumstances. In particular how to best utilise money she and her partner had saved/invested and to discuss the eventual repayment of their interest only mortgage. Ms L also had three personal pensions and it was agreed these would also be reviewed. It's what happened to these plans that is the focus of this complaint.

AIL gathered information about Ms L's objectives, circumstances and attitude to risk. Ms L's objectives were recorded in the following terms:

"You would specifically like to review your existing pensions. This objective is important to you as you want to maximise growth of your existing pensions. To ensure that they are invested in line with your attitude to risk and well diversified across a broad range of asset classes and fund managers. You would like your pension to offer you flexibility in retirement and to be passed on to your heirs in a tax efficient way. To consolidate onto one easily manageable platform. You would also like your pension and investments to be reviewed on an annual/regular basis, and the on-going servicing fee to be paid for out of the policy."

AIL recorded Ms L was 55 at the time of the advice. She was cohabiting and had no financial dependents. She was in good health. She and her partner were said to have an income of around £6,000 a month with an average monthly surplus after outgoings of about £2,000. Their home was valued at around £725,000 and they had other deposits and financial assets worth around £225,000. Their main liability was an interest only mortgage of about £300,000. Ms L says at the time of the advice it was five years until this had to be repaid.

Ms L also had three personal pensions, one with Scottish Widows and two with ReAssure. Together these had a transfer value of around £160,000. She was entitled to a state pension from the age of 67. It's recorded that she wanted to retire at 60, in around 5 years.

AIL conducted an assessment of Ms L's attitude to risk and determined her appetite was an 8 out of 10 (one being the lowest and 10 the highest scores). This was defined in the following terms:

"You would like to take a high level of risk with your investments and are comfortable with the fact that they can increase and decrease in value significantly. You are happy to take a much higher level of risk than a typical medium risk investor to look for potentially higher returns over the medium to longer term. You are comfortable with investing predominantly all of your portfolio in higher risk areas such as the stock market and accept that your capital will fluctuate in value substantially."

AIL issued its suitability report on 15 October 2021. It recommended that she switch her Scottish Widows Group Personal Pension, ReAssure Personal Pension and ReAssure With-

Profits plans into a Fidelity SIPP and its Growth 8 Portfolio. Ms L accepted AIL's recommendations and her funds were switched into the new arrangement.

Unfortunately, over the course of the following months the value of Ms L's pension funds fell. By May 2023 she says she'd lost around 13% of her retirement pot. She and her partner had similar concerns about what had happened with their investments which AIL had also advised them on. In May 2023 they raised a complaint covering all these matters. At the heart of their case was they felt they'd been misled and mis-sold products by AIL.

AIL issued its final response to Ms L and her partner on 13 July 2023. It rejected their complaint, summarising its position in the following terms:

"In conclusion, when you have experienced a poor environment for investment, where virtually no funds have been prosperous, you have to ride out the investment rollercoaster to get to the point where the markets become more conducive to making money. Whilst 3 of the last 5 years have produced losses in the wider world, under normal circumstances you would expect to make money 7/8 times out of every 10 years. It's not to say that investment prosperity is going to come to us tomorrow but over the longer term which is a recurring point of our response. Over the longer term, we remain of the view that you will be better off with us than without us. The investment returns will speak for themselves, as will our experience."

"As our risk warnings detail, markets can go up as well as down and we cannot be held accountable and you have confirmed, we have provided you with plenty of risk warnings. The risk has been appropriate and in line with your instructions, and the funds have been well chosen with high quality managers along with the appropriate diversity. Unfortunately, the nature of investing is that you cannot expect to make money every year and over the longer term the losses will be recovered, and the performance will come to you in a meaningful way."

Ms L brought her case to this Service. The Investigator who reviewed it recommended it be upheld. He concluded in the following terms:

"…I don't think AIL's recommendation to transfer the pensions into a Fidelity SIPP was suitable for Ms L. I can't say it was fair to take on the extra costs of the new plan for the reasons given. And there isn't enough evidence to show that trying to outperform the existing pensions was in Ms L's best interests with her time to retirement, especially with the view that the level of risk being taken to achieve this were beyond her risk appetite. Ms L was already appropriately invested in her existing pensions and had options to change those investments within the pensions she had. So, had Ms L received suitable advice, I think she would've likely kept the pensions as they were"

AIL disagreed with the Investigator's findings and conclusions. It rebutted a number of his findings around its assessment of Ms L's risk appetite and assumed retirement age. It believed her complaint was essentially about investment performance which was beyond its control and maintained that its advice had been suitable. In concluding AIL said:

"In summary, had the pension been performing as it was hoped and expected in different market conditions, then it is unlikely any complaint would have been made. It does not appear to us that the client was complaining about the level of risk or the higher charges, but this has been turned into the reason for upholding the complaint. As above, this would appear to be based on subjective, individual opinion and the application of hindsight rather than known, factual information and documented evidence."

As both parties couldn't agree with the Investigator's view, Ms L's complaint has been passed to me to review afresh and provide 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.

Where there's conflicting information about what happened and gaps in what we know, my role is to weigh the evidence we do have and to decide, on the balance of probabilities, what's most likely to have happened.

I've not provided a detailed response to all the points raised in this case. That's deliberate; ours is an informal service for resolving disputes between financial businesses and their customers. While I've taken into account all submissions, I've concentrated my findings on what I think is relevant and at the heart of this complaint.

I'm upholding Ms L's complaint. I'll explain why.

How does the regulatory framework inform the consideration of Ms L's case?

The first thing I've considered is the extensive regulation around the services like those performed by AIL for Ms L. The FCA Handbook contains twelve Principles for businesses, which it says are fundamental obligations firms must adhere to (PRIN 2.1.1 R in the FCA Handbook). These include:

- Principle 2, which requires a firm to conduct its business with due skill, care and diligence.
- Principle 6, which requires a firm to pay due regard to the interests of its customers and treat them fairly.
- Principle 7, which requires a firm to 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.

So, the Principles are relevant and form part of the regulatory framework that existed at the relevant time. They must always be complied with by regulated firms. As such, I need to have regard to them in deciding Ms L's complaint.

Further, COBS 2.1.1 R requires a firm to act honestly, fairly and professionally in accordance with the best interests of its clients, in relation to designated investment business carried on for a retail client. The definition of "designated investment business" includes "arranging (bringing about) deals in investments".

COBS 9.2.1R sets out the obligations on firms in assessing the suitability of investments. They are the same things that I look at when reaching a decision about whether the advice was suitable. In summary, the business must obtain the necessary information regarding: the consumer's knowledge and experience in the investment field relevant to the advice; their financial situation; and their investment objectives.

When I consider a case where someone has switched their pension funds, I look at their circumstances at the time. Why were they interested in switching? Were those wants or needs reasonable? And so, should the adviser have recommended the switch?

Each case is different, but I'd expect the switch to be in Ms L's best interests to make the advice suitable. And in this regard, I'd expect to see a comparison was made between her former pensions and the recommended new arrangement. And that proper planning had been done in relation to her income requirements in retirement.

In 2009 the Financial Conduct Authority (FCA), then the Financial Services Authority, published a checklist for pension switching that I think is still helpful today. It highlighted four key issues it thought should be focussed on:

- Charges - has the consumer been switched to a pension that is more expensive than their existing one(s) or a stakeholder pension, without good reason?
- Existing benefits - has the consumer lost benefits in the switch without good reason? This could include the loss of ongoing contributions from an employer, a guaranteed annuity rate or the right to take benefits early.
- Risk - has the consumer switched into a pension that doesn't match their recorded attitude to risk (ATR) and personal circumstances?
- Ongoing fund management - has the consumer switched into a pension with a need for ongoing investment reviews but this was not explained, offered or put in place.

Did AIL meet the regulatory obligations it was bound by when advising Ms L?

I don't think AIL met the requirements placed on it in this case. I'll explain why.

There are several documents relating to AIL's transaction with Ms L that are important to my consideration, these include the fact-finds, risk appetite questionnaire, pension and portfolio comparators, meeting notes and the suitability report it provided.

AIL's fact-find around Ms L's pension provision wasn't very detailed. At a basic level, I can't see evidence of modelling carried out by AIL which shows how the advice it gave her in 2021 came together to deliver her income requirements in retirement.

Indeed, what level of income was she targeting? And so, what did she need to achieve with her personal pensions in order to secure this? And how did the wider household position impact on these considerations? How did her existing provision and what was being proposed measure up against these metrics?

I think this analysis would've been important to Ms L being able to take an informed decision about what to do with her personal pension. But there's nothing in AIL's suitability report or fact find to speak to these matters. This is a fundamental weakness.

I find there are several further problems with its advice.

AIL was clear with Ms L that its recommendation for her to switch her three personal pensions into the Fidelity SIPP and its Growth 8 Portfolio would significantly increase the charges she incurred. It's suitability report said:

'I can confirm that you have received a copy of the O&M Consolidated transfer report and you understand that the Fidelity plan is 1.84% per annum more expensive than your existing plans (consolidated). The additional annual rate of growth (critical yield) required to provide an identical fund to your current Scottish Widow and ReAssure plans is 2.1% using an assumed rate of 1.24%. This is a Real Term Projection rate used taking inflation into account of 2% to illustrate it's worth in today's terms. The comparison is based purely on charges (includes our initial fee of 2.62% and 1% ongoing) and does not take into account investment performance. This would have the effect of reducing your pot by 32.5% should investment performance be indifferent between the two.'

The rationale for Ms L taking on increased costs was essentially that her new pension arrangement would outperform her previous plan, exceeding the drag of higher overheads. In making a comparison of performance over the previous 5 years, AIL told her:

"The O&M portfolio vs portfolio report shows that over the last 5 years the Growth 8 portfolio has grown by over around 97% whereas your existing plans (excluding the With Profits) has grown by around 28% over the last 5 years. Based on the figures in the O&M report over the last 5 years our portfolio has outperformed your current pensions by around 69%. Therefore, by transferring your pension now into an Applewood fund portfolio you would have the potential for greater growth in the long term. The With Profits fund is excluded from the performance figures as we have been unable to obtain these."

Leaving aside the comparison AIL was making was incomplete because it didn't take account of the performance of Ms L's ReAssure With profits plan (which accounted for over a quarter of her funds), the fundamental difference between her former and new pension arrangements was the increased exposure to risk she was taking on.

There are various aspects to the approach AIL took to understanding Ms L's risk appetite. The Investigator concluded the new arrangements it had recommended were beyond her risk appetite. AIL disagreed with his findings and responded in the following terms:

"The Investor Risk Profile tool the adviser completed with the client shows the chosen outcome of 8/10. There was a further meeting between the adviser and the client to discuss this to ensure her understanding. As the client went on to sign and return the document, it was our understanding she was happy to proceed with that level of risk having had chance to review all the information available to her. The Suitability Report received by the client clearly details that there had been discussions on the ATR, the clients' capacity for loss has also been discussed in detail, with the fact that the customer does have lower risk investments and savings highlighted. The client agreed to this at the time and signed all the paperwork to confirm this. We are therefore satisfied that the client's attitude to risk was accurately assessed and that she had the opportunity to advise if she disagreed with this assessment."

"Additionally, it is important to note that again, the client does have non-pension investments and, whilst most are of lower risk, they do represent additional knowledge and experience of the client, including the very high-risk investment of shares held in oil companies. It is also reasonable to expect that any investor that has experienced the impact of Brexit and the Pandemic on existing investments shortly before the period of advice, would be well aware of the volatility of investments. We wholly disagree that Ms L gave the answers to the risk profiler without understanding them. Ms L had also previously worked for an international law firm before setting up as a Director of her …company. We believe that this would indicate a level of education and professional standing such that Ms L should understand the meaning of the questions posed to her, and in addition, would understand the importance of seeking clarification if she did not understand at any point. There were many opportunities for Ms L to do this before agreeing to proceed."

"The points raised regarding the timescale to retirement is also something we disagree with. The selected retirement age of 75 was discussed and detailed in the suitability report, which is a summary of the conversations and advice being provided. Ms L's State Pension Age is 67 and it is unlikely her pensions would provide sufficient income for her to retire at age 60, if based solely on her assets so it is clear this is an unlikely retirement age, regardless of whether a client wants to retire early or not. The only rationale for being able to do so is that her partner of 25 years…earns £73k pa and has 21 years membership of [a] DB pension scheme, but this only adds to her capacity for loss with her pension if this is the case. Therefore, the retirement date and investment term is not 5 years, but at least 12, and taking the agreed level of risk with a long-term outlook is therefore not unsuitable."

“Additionally, Ms L is self-employed and typically, self-employed people don’t retire when they think they will and typically remain working for longer. As such, the timescale for the investment to 75 is not unreasonable and, therefore, the higher risk funds are not unreasonable either. As self-employed clients also have more fluctuating needs, the recommendation to immediately switch into flexi-access drawdown and the objective of having flexibility in retirement is also not inappropriate.

Turning first to the attitude to risk questionnaire that AIL completed with Ms L. I note the assessment was signed by her on 1 November 2021. AIL says the actual assessment was conducted on 29 September 2021. Its pension switching report was dated 6 October 2021 and the suitability report it produced for her was delivered on 15 October 2021. It also provided separate advice and a suitability report for Ms L and her partner on 24 November 2021 in respect of certain investments it was recommending.

I’ve not seen that a separate attitude to risk assessment was done in respect of Ms L’s pension arrangement and the investments she was being advised to make with her partner. I think this is a weakness in AIL’s approach. Although viewing a person’s assets in the round is important, so too is understanding the nature of those assets. Pensions are to provide an income in retirement, whereas investments are often for other purposes. They often attract a different assessment of risk appetite.

I’ve no doubt that the answers to the questionnaire AIL provided to Ms L delivered a result which indicated she had a high level of risk appetite. But certain responses might suggest that the focus of her responses were on the investments she and her partner were making. For example, it’s stated that she was investing less than 25% of her assets (excluding the value of her home). That’s clearly not the case when considering the value of her pensions at the time.

AIL asserts Ms L was an experienced legal professional who went on to establish and direct her own company and so would’ve understood the risk assessment questions and process. I don’t find that her professional background means she was particularly knowledgeable on matters of pensions, retirement planning and investments. Indeed, I note on the original risk assessment form AIL noted that while she’d had a pension for 25 years and understood the basics, she wouldn’t be classed as an expert. I agree.

As AIL acknowledged in the pension switch suitability report it gave Ms L, understanding a person’s capacity for loss is a crucial element of the overall assessment of what exposure to risk someone can take on. It said:

“Having established your attitude to investment risk i.e. the risk you are willing to take, it would be a mistake not to consider your capacity for loss i.e. the risk you are able to take. To put it another way, as the recommendation in this report is for investments that can fluctuate in value and have a potential to lose some of their value, at any point during the term of the investment and importantly, potentially when you want to access the funds, then we need to assess and agree your ability and willingness to absorb such potential losses.”

“In this respect, we established the following: You have sufficient funds invested in low risk assets and cash, to balance against investing these funds in the stock market; You understand that there is a potential that these investments may fall in value, but considering your financial circumstances overall, I am confident you could absorb any losses without a material effect on your standard of living; you have confirmed that you would be comfortable with this.”

I think there are flaws in AIL’s assessment here. Excluding the value of Ms L and her partner’s home, the fact-find records they had £225,000 of assets (deposits, stocks and shares). But it also notes they had an interest only mortgage with outstanding capital of

£300,000, which I understand at the time had around 5 years until repayment. And notes from the initial meeting AIL had with Ms L and her partner makes clear they wanted to remain in the property.

I think the information AIL captured from Ms L indicated a low capacity for loss in respect of her pension. Aside from a state pension the funds it was advising her to switch into a SIPP and high risk investments was her only provision for retirement.

Part of AIL's justification for Ms L investing her pension funds in higher risk investments was the long-term nature of the arrangement. It recommended her pension plan be written to the age of 75. And it has recently asserted that self-employed people often don't retire when they say they will and typically work longer, and so it's assumption of the horizon it recommended was reasonable.

The problem for AIL here is that information it gathered from the time of the advice it provided Ms L was quite clear about her retirement plans. For example, notes from the initial meeting it had with Ms L records she wanted to retire at 60. The pension planning fact-find it conducted asked at what age she would like to retire, what age she anticipated retiring and the oldest age she would wish to retire – each time she responded 60.

It may've been the case that Ms L could never have afforded to retire at 60. We don't know because AIL never conducted any retirement income planning at the time. Had it done so, this would've flushed out better what her options were. AIL can't now retrospectively assert what would've been the case at the time. In the same way I put very limited weight on the attitude to risk questionnaire that Ms L has recently completed showing that her appetite for risk is low. I find both parties have made certain of their arguments based on hindsight.

AIL's role wasn't to facilitate Ms L's wants, but was to understand her needs. It was in a good position to have analysed, tested, challenged and advised her about what was in her best interest for retirement planning. It knew pension pots built up over many years are to provide for a retirement income. It had a duty of care to ensure she was fully informed about the choices she was making.

I don't find AIL's response to the Investigator's findings and conclusions compelling for the reasons I've already set out. Overall, AIL hasn't done enough to demonstrate the switch of Ms L's Scottish Widows and ReAssure pension plans into a more costly SIPP and higher risk investments was clearly in her best interests.

Putting things right

I'm upholding Ms L's case. So, she needs to be returned to the position she would've been in now - or as close to that as reasonably possible – had it not been for the failures which I hold Applewood Independent Limited responsible for.

If Applewood Independent Limited had provided suitable advice, I don't think Ms L would've wanted to increase her exposure to risk. And I think it's more likely than not she would've kept her existing pension arrangements in place.

I understand Ms L remains in the SIPP and investments recommended by AIL.

So, Applewood Independent Limited needs to provide redress as follows:

Calculate a notional value for Ms L's pension funds as if they had remained with her previous providers*. And compare the result with the actual value of her SIPP and the investments recommended by AIL, as at the date of settlement.

I’m not aware of the detailed position regarding any additional contributions Ms L made to her SIPP, or whether she has been taking benefits from her pot. After confirming the detailed position, then the value AIL obtains or the calculations it makes should assume any such adjustments would still have occurred and on the same dates.

If the actual value is greater than the notional value, no compensation is payable. If the notional value is greater than the actual value, there is a loss and compensation is payable.

If there is a loss, Applewood Independent Limited should pay into Ms L's pension plan, to increase its value by the amount of the compensation and any interest. Payment should allow for the effect of charges and any available tax relief. It shouldn’t pay the compensation into the pension plan if it would conflict with any existing protection or allowance.

If Applewood Independent Limited is unable to pay the compensation 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’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 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%.

Applewood Independent Limited should provide the details of the calculation to Ms L in a clear, simple format.

** I agree with the Investigator’s assessment that if Ms L’s previous providers are unable to calculate a notional value, Applewood Independent Limited should use the FTSE UK Private Investors Income Total Return index as a reasonable proxy, given her previous asset spread as set out in its Pension Switching Report of 6 October 2021. The 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.*

There is guidance on how to carry out calculations available on our website, which can be found by following this link: https://www.financial-ombudsman.org.uk/businesses/resolving-complaint/understanding-compensation/compensation-investment-complaints. Alternatively, just type ‘compensation for investment complaints’ into the search bar on our website: www.financial-ombudsman.org.uk.

My final decision

For the reasons I’ve already set out, I’m upholding Ms L’s complaint. As such, I require Applewood Independent Limited to put things right in the way I’ve directed.

Under the rules of the Financial Ombudsman Service, I’m required to ask Ms L to accept or reject my decision before 20 August 2024.
Kevin Williamson
Ombudsman