DRN-4793411

Financial Ombudsman Service

The complaint

Mrs F and Mr R complain The Devereux Partnership LLP ("Devereux") gave them unsuitable investment advice, causing them financial loss and inconvenience. In particular they say the recommended portfolio was too risky and they only wanted to invest for a short time to build up funds for house purchase, but the portfolio losses prevented this house purchase.

What happened

Our investigator summarised the complaint circumstances. In brief summary:

Devereux met Mrs F and Mr R in June 2021. They were around 50 and renting. They had about £340,000 from the sale of their homes. The sort of home they wanted to buy could cost £650,000 for which they would need to borrow around £325,000. They were unable to borrow this at the time. Mrs F and Mr R say this is because their earnings were too low due to lockdown. Devereux says it was also because they needed at least three more years of records to prove they had sufficient earnings, due to being self-employed.

Mrs F and Mr R invested around £333,460 on Devereux's advice into an investment portfolio including two ISAs. A suitability report dated 15 September 2021 was produced after the investment was made but it wasn't given to Mrs F and Mr R at the time – only after they complained in August 2023 - for which Devereux offered them £250 redress. It also offered them £4194 for losses arising from a delay in making a fund switch for them.

Our investigator thought the complaint should be upheld and found - in brief summary:

- The suitability report wasn't sent to Mrs F and Mr R as it should have been.

- Although classified as medium risk investors, the portfolio Devereux recommended to Mrs F and Mr R was invested 75% in funds risk rated as six on a seven point scale, with 10% in risk five and 15% in risk four. In 2022 Mrs F and Mr R became aware of one risky fund and switched out of it but this still left a large proportion (55%) in such funds.

- Devereux should've advised Mrs F and Mr R against investing 98% of their funds, which was far too much for inexperienced investors. Only the £6360 emergency fund was left.

- Mrs F and Mr R say they only wanted to invest for two years. Devereux's advice letter referred to a medium to long term investment of five or more years, but this wasn't made clear to Mrs F and Mr R as they didn't get the letter until they complained in 2023. Given this, the evidence doesn't confirm that they wanted a medium to long term investment.

- Devereux should compare the performance of Mrs F and Mr R's portfolio with what they would've had if they'd invested instead in an portfolio where half made a return equal to a risk free return from fixed rate bonds, and half made a return equal to the return from the FTSE UK Private Investors Income Total Return index (more than half of which is usually in shares with the remainder in bonds and some other assets). It should also pay £500 for inconvenience and distress caused to Mrs F and Mr R by these matters.

Mrs F and Mr R replied to say that they crystallised their losses and withdrew their funds as they needed to buy a property, and that their losses had meant they needed to take out an interest only mortgage. They say the part of their complaint that Devereux upheld should be upheld regardless of anything else. They also say the initial set up fee should be refunded to them given that the advice and work done for them by Devereux was found questionable.

Devereux replied rejecting our investigator's conclusion. In brief summary:

- It didn't accept Mrs F and Mr R only wished to invest for one or two years. On their risk questionnaire they'd put their investment timeframe as *"0-5 years possibly longer"* and also that they *"wanted to receive higher long term returns"* and *"higher long term returns growth rather than 1 year returns"* and said they would 'delay their objective' if there were a market downturn. Also in May 2021 they said they would pay rent in *"the medium term"*. Mrs F and Mr R referred to medium and long term a number of times. They never suggested they wished to invest for one to two years. There were enough clues that it wasn't a one-to-two-year investment.

- Also Mrs F and Mr R had said in 2021 they wanted to invest *"to get a big return"*. Their risk questionnaire said they were willing to *"take a lot more risk with some of the money"* and were 'comfortable with a loss of 5-15%' and for a 20% loss would *"wait for the portfolio to recover"*. Also Devereux was honest with them about the downside potential.

- Mrs F and Mr R told Devereux how much they wanted to invest, and Devereux told them they should invest whatever amount they were happy with.

- The market downturn in 2021 wasn't expected by anybody. Insofar as the portfolio fell in value, the risk of investing was highlighted in the risk questionnaire.

- The funds when blended together don't equate to high risk. The overall risk comes out as six out of ten based on real life volatility even though the majority of funds are rated as six out of seven on that crude measure. The advice was suitable based on the risk questionnaire and the discussions at the time.

- If the above is not accepted, a recommendation that might have been deemed suitable would have been a risk rated managed fund investing in a mix of equities, bonds and the money market. The average mixed investment fund with 20-60% in shares, and a risk reward rating of four out of seven, would have lost 2.47% from when they invested until they asked for the Devereux adviser to stop looking after the portfolio. This compares with a loss of 9.12% for the recommended portfolio over the same period.

As the matter couldn't be resolved informally it has been passed to me to decide.

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.

Having done so, I've arrived at the same conclusion as our investigator and for broadly the same reasons. In particular my view is that the portfolio Mrs F and Mr R were advised to invest in was too risky given their risk attitude and circumstances.

If 'medium risk' is in the middle of a risk scale, and a balanced investor is someone also wanting a middling sort of risk on that scale, then on a scale of one to seven a medium score would be four. On a scale of zero to seven a medium score would be four or five. In either case a portfolio with only 25% of its funds scored at risk three, four or five out of seven, with the rest at six out of seven, on the face of it would appear to involve excessive risk.

I note the risk questionnaire's ten-point scale described one to three as low and four to seven as medium with eight to ten as high. Level five is described as a *"balanced investor"* accepting *"a degree or risk while including some security of capital"* while accepting risk of loss in return for a potentially higher return. The suitability report refers to Mrs F and Mr R as accepting average risk. Level six is described as *"higher than average degree of risk"* with *"greater exposure to equity investments".* So if I were to accept that the portfolio risk level was less than the average score of its constituent funds, which was eight out of ten (5.6 out of seven), and reduced to six by the portfolio effect like Devereux says, this still exceeds the risk level implied by the risk attitude description in Devereux's suitability report.

I note that the allocation to UK and international shares was the main thing raising portfolio funds' risk to level six. I accept diversification of a portfolio will tend to reduce risk – and I note the funds invested in different regions. But I also note share price moves in different regions can be positively correlated in market downturns - what causes prices to fall in one region might also cause prices to fall in other regions. That said, I give some credit to the view that risk elements that gave funds an average risk score of eight out of ten will have been balanced down somewhat by the portfolio effect of combining the funds. But in light of all I've said above, I don't think this was sufficient to bring the risk level within a range that would've been suitable for Mrs F and Mr R given their risk attitude and circumstances.

In saying this I also note the risk questionnaire offered a notional choice between portfolios with various levels of volatility listed from A (the most stable with a yearly range on £100,000 of £110,000 to £96,000) to E (the most volatile with a return range of £160,000 to £70,000). Mrs F and Mr R circled A and B (B's range was £120,000 to £90,000). This choice favoured volatility at the lower end of the ranges offered, rather than the middle or upper end.

I note also that under the heading 'Capacity for Loss', when asked on the questionnaire what level of fall in a year would concern them, Mrs F and Mr R chose 5% to 15%. So this choice indicates potential concern with a fall of as little as 5% or as much as 15% in a year – which isn't the same as saying they were comfortable with that level of volatility or potential loss.

In saying this I don't overlook that the suitability report said: "*you are willing and able to accept the potential volatility of the investment and the possible loss that may be incurred".* It said this in a section that also said *"…your capacity for loss… would highlight the amount of money you could actually afford to lose when making your investment"* and gave an example of a 5% or 15% fall in markets causing a £10,000 investment to fall by the same percentages (£500 and £1500). As the report wasn't sent to Mrs F and Mr R at the time, I can only give it limited weight. But it isn't obvious to me this is saying the recommended portfolio was one where a 1% market fall would lead to a 1% loss in the portfolio, or that the 5% to 15% figures were indicative of the expected volatility of their portfolio and what they would be willing or able or comfortable in accepting. Also when offered different levels of portfolio volatility, they chose ones (A and B above) whose largest potential one year downside was less than 15%.

Overall, consideration of the particular answers given by Mrs F and Mr R on their risk questionnaire doesn't in my view add weight to or support the idea that the portfolio's investment risk level wasn't excessive for Mrs F and Mr R's risk attitude and circumstances – or that they had a *"medium"* or *"balanced"* risk appetite that was somehow at the upper rather than lower range of the risk levels that such descriptions might cover.

I'd add that the savings Mrs F and Mr R held back were small in the context of the losses the portfolio might suffer – so these doesn't provide much reassurance as to Mrs F and Mr R's willingness or ability to accept potential risk and loss. I note £6000 in savings might help in the context of a £1500 to £500 annual loss, like that touched on in the suitability report for a

£10000 investment, but on Mrs F and Mr R's investment of over £330,000 even a 5% loss would be more than £16000, and well in excess of their retained savings figure. So those savings didn't materially increase Mrs F and Mr R's ability to take risk or add to the merits of advising them to take more rather than less risk.

I'd also add that the degree of risk suitable for a given risk appetite will vary with the investment time horizon. A short time horizon of less than five years would usually rule out a significant allocation to shares for those without more adventurous risk attitudes. A medium to long term time horizon allows more scope to recover investment costs, ride out temporary falls in prices and benefit from earnings growth that might be expected over the medium term. Holding shares over shorter time horizons increases the risk involved. With all this in mind I turn to the question of Mrs F and Mr R's planned or expected investment term.

The suitability report sets out Devereux's understanding of the position, although it didn't share this with Mrs F and Mr R. It says: *"You are looking to invest this available cash for the future in order to achieve potential capital growth greater than that offered by cash deposits and build your lump sum to enable you to buy a house in due course. In order to give the investment sufficient time to meet your objectives, I have suggested a time frame of five years. This fits in with your approximate time frame but might wish to draw the money sooner if you find a suitable property and the investments have done well."*

I note this contemplates the possibility of drawing the investment after less than five years. I accept Devereux's point that the evidence from the time doesn't support the idea that Mrs F and Mr R specified a term of only one or two years, but at the same time it doesn't support the idea that they had a settled notion of keeping the investment for at least five years. On their risk questionnaire Mrs F and Mr R selected *"Less than five years",* adding a written note of *"possibly longer".* They didn't select the option, which was there, of *"Five to ten years"*. In my view this plainly suggests that Mrs F and Mr R thought it possible the investment might run for less than five years. I give this evidence more weight than what the Devereux adviser recalls now of the discussions, given the questionnaire was answered by Mrs F and Mr R themselves and at the time the investment was being discussed rather than later on.

Also with regard to Mrs F and Mr R saying they were willing to delay their objective if the investment did poorly, I note the other available questionnaire answers were *"Invest more money"* – which wouldn't have been a practical option given how much of what they had they were investing already – and *"Take more risk in order to achieve your objective"*. So the selection of *"Delay your objective"* merely reflects the reality that if the portfolio did poorly this would be what Mrs F and Mr R would have to do, if one sets aside the other option of gambling more by taking on more risk, which would hardly be sensible in that scenario.

Also with regard to what Devereux says about Mrs F and Mr R wanting long term returns, this answer was to a question that related to the risk and volatility they might be willing to take. Their answer included that they were willing to accept *"reasonable levels"* of volatility. The other answers offered were to say they were *"risk averse"* including that *"stable but low returns are required"* or to say they wanted to *"maximise long term returns and accept reasonable levels of volatility".* So what they were saying in this question was they wanted a middling sort of volatility and return. I don't think it can be fairly inferred from this answer that Mrs F and Mr R were indicating that they wanted an investment term of five years or longer – particularly given the answer they gave when asked about this plainly elsewhere in the risk questionnaire. Also I note in passing that the question doesn't explain that *"long term"* would mean more than five years anyway, which only reinforces my view already explained above.

So in my view it is plain that there was some uncertainty over the potential investment time horizon – and there was a possibility the investment term might be shorter than five years. In view of this I consider the risk Mrs F and Mr R could suitability be advised to take needed to be lower than would otherwise have been suitable. In my view this reinforces my conclusion that the risks involved in the portfolio Devereux recommended were excessive for their risk attitude in their circumstances.

With this in mind, while I agree with Devereux that the evidence we have does suggest there was also a possibility that the investment might go on for five years or more – and so some allocation to risk assets wasn't entirely unreasonably – in my view the allocation did need to be tempered given the chance that the investment term might not last as long as that.

I'd add that risking funds needed for house purchase is a risky enterprise in itself. Any loss of capital wouldn't be a loss of spare capital that wouldn't directly impact their lifestyle Such losses would have direct impact by increasing the time they would need to spend in rental accommodation or changing where or in what sort of house they could eventually afford to live. So losses could have a potentially very significant impact. It seems to me this suggests that for any given risk attitude, an investment approach on the more cautious end of it was advisable. This reinforces my view that the portfolio was too risky given Mrs F and Mr R's risk appetite and circumstances.

With all this in mind I find the portfolio recommended did carry too much risk. I also find that the alternative of an investment with up to 60% in shares, would also carry too much risk given the particular circumstances and objectives of Mrs F and Mr R, as discussed above. In my view the benchmark proposed by our investigator, which would set the shares and hedge funds component at (very broadly) half of that in the mixed managed fund class Devereux has proposed, is more appropriate.

I note Mrs F and Mr R have cashed in the portfolio. So the loss assessment needs to end at the date the portfolio ended, rather than running to date. Also interest on any loss found at the portfolio end date needs to be added from that date to the date redress is paid, to account for the time that has passed since the portfolio ended.

With regard to Mrs F and Mr R's claim for a refund of the set-up fee, the suitability report said Mrs F and Mr R agreed to pay just over £5000 for the advice, being just over 1.5% of what they were investing. This was *"deducted directly from the investment amount"*. The redress calculation proposed by our investigator didn't make provision for deducting such a set up or advice charge when calculating the benchmark fair value – so the full investment amount (before and without deduction of a £5000 set up or initial fee) would be used to calculate this value. The principle, with which I agree, is that as the advice was unsuitable, the calculation shouldn't deduct from the redress the charge made for that advice. So insofar as the charge contributed to a financial loss (judged by what Mrs F and Mr R would've got from an appropriate portfolio represented by the benchmark) this will effectively be returned within the redress calculation. So there is no need for an award to refund that separately. Also I think this is a fair approach to redress, regardless of other offers that have been made.

So, to conclude, in light of all I've said above I uphold this complaint for the reasons and on the basis I've outlined above.

Putting things right

Fair compensation

In assessing what would be fair compensation, I consider my aim should be to put Mrs F and Mr R as close to the position they would probably now be in if they had not been given unsuitable advice.

I take the view that Mrs F and Mr R would have invested differently. It is not possible to say *precisely* what they would have done differently. But I am satisfied that what I have set out below is fair and reasonable given Mrs F and Mr R's circumstances and objectives when they invested.

What must Devereux do?

To compensate Mrs F and Mr R fairly, Devereux must:

- Compare the performance of Mrs F and Mr R'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.

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

- Pay to Mrs F and Mr R £500 for distress arising from the extra falls in the portfolio value that arose due to its excess risk, as well as inconvenience arising from this and from failings like not receiving the suitability report on time.

Income tax may be payable on any interest awarded.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Portfolio including the ISAs	No longer in force	For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds	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 portfolio would have been worth at the end date had it produced a return using the benchmark. The starting investment amount is the full amount paid into the portfolio (including the ISAs) before any deductions.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, Devereux should use the monthly average rate for one-year fixed-rate bonds as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

Any withdrawal paid to Mrs F and Mr R 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 were a large number of regular payments, to keep calculations simpler, I'll accept if Devereux totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically. I'm not sure there were any withdrawals, but I make this provision for completeness.

Why is this remedy suitable?

I have decided on this method of compensation because:

- Mrs F and Mr R wanted capital growth but could only be suitably advised to take a small risk to their capital given their circumstances and risk appetite.
- The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to their capital.
- The FTSE UK Private Investors 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 prepared to take some risk to get a higher return.
- I consider the degree of risk suitable for Mrs F and Mr R was in between, as they could be suitably advised to take a small level of risk, that included some security of capital, in pursuit of their investment objective. So the 50/50 combination would reasonably put them into that position. It does not mean they would have invested 50% of their money in a fixed rate bond and 50% in some kind of managed or index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of return Mrs F and Mr R could have obtained from investments suited to their objective and risk attitude.

My final decision

I uphold the complaint. My decision is that The Devereux Partnership LLP should pay the amount calculated as set out above.

The Devereux Partnership LLP should provide details of its calculation to Mrs F and Mr R in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs F and Mr R to accept or reject my decision before 28 February 2025.

Richard Sheridan
Ombudsman