DRN-5593804

The complaint

Mr A has complained about the advice he received from Fidelius Ltd ('Fidelius') to sell suitable investments that increased his capital gains tax ('CGT') liability. He also complains that his account has been subject to extreme trading.

Mr A is represented in bringing his complaint, but for ease of reading, I shall refer to 'Mr A' throughout my decision.

What happened

Mr A had been a client of Fidelius for many years and held a taxable portfolio ('GIA'), ISA and pension. In 2022 he agreed to three funds being sold – Artemis Income, Invesco UK Equity Income and Threadneedle American Select – because he was advised they were too high risk for him – which gave rise to a capital gain of £116,746. Mr A had already made his adviser aware he was selling a property later that year. Mr A was then advised by his new financial adviser that the three funds wouldn't have had a significant impact on the overall risk of his portfolio, and he would have been better off selling them over several tax years.

As a result of the above, Mr A looked further into the management of his portfolio, and he found there had been extreme investment turnover within his portfolio for many years averaging at £500,000 per year. He said this has led to poor performance, additional charges and unnecessary and significant CGT.

Mr A raised a complaint with Fidelius. It didn't think the complaint should be upheld. It said;

- Mr A had been informed that a capital gain would arise on the sale of the three investments, and he accepted that. So, he made a fully informed decision.
- The three funds were too volatile for Mr A's Balanced risk level so it was suitable to recommend they be sold.
- Because of Mr A's circumstances with holding property and shares, it wasn't possible to achieve Mr A's investment objectives and avoid CGT on the sale of the funds. The only other option would have been to hold them until Mr A's death, but he was accepting of tax in order to invest. The sale was suitable from a tax perspective.
- There were no additional costs for the advice.

Fidelius later responded to further concerns including the quantity of trading on Mr A's account;

- Mr A had been with Fidelius – and the predecessor business – since 2007 and his GIA and ISA were held on a third-party platform. Mr A moved his GIA and ISA to the Parallel Investment Management ('PIM') discretionary fund managed ('DFM') service in April 2013 and Mr A agreed to crystallise £20,000 of gains in order to move to the PIM portfolio.
- In 2015 Mr A transferred his pensions onto the third-party platform and invested in the DFM PIM portfolio. He realised a small gain to fund his ISA.

- In 2020 PIM was bought by Pacific Asset Management ('PAM') and all funds were sold to realign with PAM's investment strategies. A gain was cystallised on the GIA.
- In 2022 Mr A was advised to move the last three funds not held in the DFM into the GIA PAM DFM model in line with his agreed risk profile.
- All trades were executed under the DFM mandate to manage the portfolio which Fidelius wasn't responsible for.

Mr A wasn't happy with the outcome and brought his complaint to the Financial Ombudsman Service. Fidelius said any complaint about the management of the portfolio should be directed at the DFM manager and the complaint about the level of trading was made too late.

A fellow ombudsman decided that this service could consider the complaint. It hadn't been made too late under the rules that apply, and Mr A's relationship was with Fidelius, so it was responsible for the suitability of the discretionary portfolio and the DFM acted on its instructions.

Our investigator went on to consider the merits of the complaint and thought it should be upheld in part. He said;

- Three complaint points had been raised that Fidelius hadn't had the opportunity to respond to so they didn't form part of this complaint and Mr A would need to raise them with Fidelius in the first instance.
- He didn't think the volatility of the three funds in isolation was detrimental to the portfolio to the extent they should have been sold. Fidelius didn't hold evidence to demonstrate their impact on the whole portfolio.
- Mr A had told his adviser he was going to sell property in 2022. In 2013 Mr A was only willing to crystallise £20,000 of gains to move the funds to PIM.
- Fidelius had previously advised against selling the funds because of the CGT. Advice was then given to sell the funds knowing they would incur a CGT liability and a general disclaimer about CGT was insufficient. In the context of the portfolio the ten-year volatility and asset allocation didn't justify the advice to sell the funds. Any volatility of the funds didn't outweigh the CGT liability.
- Despite Mr A's objectives and it being impossible to achieve those without CGT being payable, the investigator wasn't persuaded there was a pressing need to dispose of the funds and thought this complaint point should be upheld. He outlined how that should be put right.
- With regard to the level of trading he outlined the regulator's definition of 'churning' and the regulations and guidelines about that.
- Fidelius nor PIM or PAM charged for investment switches. But they did result in CGT, so the investigator looked at the turnover to see whether they were carried out in Mr A's best interests.
- More recent turnover was low as PAM held funds within its own Open Ended Investment Company ('OEIC') so trading wasn't visible. High turnover in 2020 was because of PAM realigning the portfolio with its own. The investigator was satisfied it was likely the transactions were part of the DFM's strategy, so in his best interests and not to generate commission.
- CGT was reasonably incurred as a result of the DFM manager pursuing its mandate and he couldn't see the DFM manager did anything wrong or mismanaged the investments. Mr A wanted a DFM service and bearing in mind the size of his portfolio

a reasonable capital gain would be expected.

Fidelius didn't agree. It didn't think the full refund of CGT for the sale of the three funds was fair. It had told Mr A the CGT that would arise on the sale of the funds and unless Mr A kept the funds until his death, he would have had to have paid CGT at some point, and it potentially prevented that liability from increasing. Fidelius didn't create the liability, and the proposed redress removed a large CGT liability which would have remained.

Fidelius' points didn't change the investigator's opinion.

Mr A also responded about the redress and other points. The investigator had said if the DFM portfolio had outperformed the funds sold, that amount could be deducted from any redress so logically if the DFM had underperformed the same would apply.

As the complaint remains unresolved, it has been passed to me to decide in my role as ombudsman.

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.

After doing so, I've reached the same conclusions as the investigator and broadly for the same reasons. I'll explain why.

I'm aware I've set out the background to this complaint in less detail than the parties and I've done so using my own words. The Financial Ombudsman Service was set up to be a quick and informal alternative to the courts. And the purpose of this decision is to explain what I think is fair and reasonable in the circumstances, not to offer a point by point response to everything the parties to the complaint have said. So, I will not refer to every submission, comment, or relevant consideration. Instead, my decision sets out what I think are the most important points to explain my decision in a way that is intended to be clear and easy to understand.

Where I have incomplete or contradictory information or evidence, I need to base by decision on the balance of probabilities and what I think most likely happened.

<u>Disposal of the three funds</u>

Mr A had held the three funds outside of the discretionary managed service portfolio he held with Fidelius. Fidelius was aware of the three funds, their value and the CGT position of those funds as referred to in correspondence with Mr A.

The October 2020 'Desktop Review' carried out by Fidelius refers to the three funds as being nearly 100% exposed to equity whereas its ideal for a medium risk investor was 67%. But it went onto to say that while this was more than Mr A's risk tolerance, his;

> 'high capacity for loss allows you to take such risk without impacting your lifestyle'.

It also said;

> 'owing to the large level of gain on the underlying funds of the GIA, we have been unable to make any switch or sale recommendations since selling down your existing holdings will give rise to a tax liability.'

However, this was to be discussed at the next review;

> 'since switching into a more suitable investment strategy would be appropriate, providing you are willing to accept the tax consequences in doing so.'

In the 3 May 2022 annual review, Mr A was advised to sell his three funds – valued at just under £215,000 – as they exposed him;

> 'to a higher level of risk than suitable for your agreed balanced risk category.'

So, it was recommended that the funds were sold and switched into the Balanced Growth Portfolio which was suitable for Mr A's balanced risk strategy. This was because Mr A was a balanced risk investor and;

> 'investments in this category could hold up to around 70% in the equity markets (shares), with the balance held in other asset types which historically have been considered less risky'.

At the time, Mr A had recently sold a property for £1.9m that fell into the previous tax year, but another was on the market for £2.3m to be sold 'soon.' Mr A agreed to the three sales on 5 May 2022 which incurred a capital gain and which Mr A has now complained about.

I've thought very carefully about this complaint point. It's clear from the Annual Review document of 3 May 2022 that Mr A was informed the sale of the three collective investments would give rise to a substantial gain for capital gains tax purposes of around £133,000 and yet Mr A agreed with the investment recommendation. So, bearing this in mind and as its recorded Mr A was an experienced investor – which I wouldn't disagree with, and this was an advised sale – I've looked at the reasoning for the investment advice given and which Mr A accepted as a reason for selling the funds.

The three funds represented just under ten per cent of Mr A's overall portfolio of around £2.6m, excluding his investment property. Fidelius itself has said that because of this, the three funds were 'unlikely to have a major impact on the risk profile of his whole portfolio.' However, it said the priority at the time was Mr A's wish for DFM within his risk profile and the advice to sell the funds was in line with that. In making his complaint, Mr A has said that if he had been made aware that keeping the funds wouldn't have pushed him into a higher risk category, he wouldn't have sold them, particularly in a year when CGT was such a problem. He could have sold the funds over several years by utilising his annual CGT allowance.

Mr A has said that his own research – using an analytical tool – indicated the 'risk score of the portfolio changed from 56 out of 100 to 59 out of 100 following the advice.' Fidelius has told us it doesn't hold evidence to demonstrate the impact of the three funds in relation to Mr A's total portfolio but its response to the complaint, as quoted above, suggests the three funds wouldn't have had a significant impact on his overall risk rating but I have considered this further.

Fidelius' own acceptable 10-year volatility for a medium/balanced investor was stated as being between the range of 8.3% - 11.8%. Fidelius has provided fund factsheets for the three funds prior to the May 2022 recommendation as well as third party analysis of their volatility over ten years;

Fund	10 year volatility	Value
Artemis Income Fund I Acc	11.93%	£56,638
Invesco UK Equity Income Fund	13.56%	£45,307

Threadneedle American Select	13.73%	£141,605
Weighted Average	**13.27%**	

I accept higher volatility – the fluctuation in the price – can be an indicator of higher risk, particularly in the shorter term and its clear the Artemis fund was only just marginally above Fidelius' acceptable level of volatility but Invesco and Threadneedle were two percentage points higher. However, Mr A had held the three funds for over ten years and all of them were showing a healthy gain at the time of the advice and he had been happy to retain the funds because his 'high capacity for loss allows you to take such risk without impacting your lifestyle.'

Fidelius has said the motivation for the sale recommendation was for the resulting proceeds to be invested in the DFM portfolio which was in line with Mr A's requirements. However, Mr A has complained that it was the higher risk nature of the funds that was the reasoning behind the sale recommendation, and he wouldn't have gone ahead with the sales if he had been made aware that retaining them wouldn't have pushed him into a higher risk category.

Looking at all the correspondence I think it's more likely Mr A's understanding of the reason for the sale is the correct one as Fidelius has consistently referred to the three funds as being higher risk than Mr A's acceptable level of risk – it was the CGT constraints that prevented any sales – but it was concluded in May 2022 that the funds exposed him 'to a higher level of risk than suitable for your agreed balanced risk category.'

However, Fidelius has said the three funds were 'unlikely to have a major impact on the risk profile of his whole portfolio' and bearing in mind the size of Mr A's portfolio, I'm persuaded that is more likely. This leads me to question why the sales were recommended, particularly in a tax year when Mr A was selling a property, and I'm not persuaded that Mr A's wish to have the funds under a DFM mandate would have overridden his preference to keep CGT as low as he could.

Mr A has said that he instructed Fidelius to limit any CGT in any tax year to £20,000 but I can't see any reference to this. There is mention in the meeting note of 29 August 2013 referring to the move of the GIA to PIM and that Mr A was 'keen for the funds to start to receive discretionary management and he is prepared to crystallise up to £20,000 in gains in order to achieve this.' At the time its recorded other funds with large gains were to be retained and gradually moved over in the next two or three years while trying to keep the CGT as low as reasonable. But I can't see that instruction extended to all tax years.

Looking further at Mr A's tax position, I accept the May 2022 Annual Report suggests that Mr A refer to his accountant if he wasn't sure about his position and that Fidelius wasn't a tax adviser, but I don't think that makes any difference here. I say this because it was already recorded in the Annual Report that Mr A had a rental property on the market for over £2.3m which he hoped would be sold soon. So, hopefully within the tax year, which proved to be the case, and was the same tax year as the proposal to sell the three funds. The adviser was clearly aware of this at the time the advice was given to sell the three funds where it was known a capital gain would be incurred. So, with both going ahead Mr A was liable for a larger CGT bill which could otherwise have been reduced if the three funds hadn't been sold.

I accept that with the size of Mr A's portfolio it was unlikely that in the main, there would be any year in which the CGT allowance wasn't fully used which raises the question about when would have been a good time for Mr A to have sold the funds. But Fidelius was aware of the CGT position and could have managed that potential liability over several years as it did in 2013.

In response to the investigator Fidelius has argued that by upholding the complaint and awarding Mr A the amount of CGT paid, this removed from Mr A the inevitability that tax would be payable on the gains within the three holdings at some point. And it said it wasn't Fidelius that created the gain.

I agree with the point Fidelius is making here. Mr A is now in a position where the capital gain incumbent within the three funds has been removed. But it ignores the fact that Mr A wouldn't have carried out the sales at the time but for the advice he received from Fidelius which cystallised that gain and which I think was unsuitable advice. Mr A had a large portfolio of assets, and while I accept its recorded he did want to increase his monthly income, there's nothing to suggest that he would have needed to sell the funds to finance his lifestyle or need a boost to his capital that would have caused him to sell the funds.

Fidelius has made the point the only way to avoid paying capital gains tax on the funds was if Mr A held them until his death. But looking at his portfolio, I see no reason that may not have been a possibility, at which point they would become liable to inheritance tax rather than capital gains tax. From what I have seen of Mr A's financial circumstances and the fact that Mr A was 69 years of age at the time of the sales, I don't think it's unreasonable to say Mr A did have the option of retaining the funds during his lifetime.

Overall, I'm persuaded that Mr A was advised to dispose of the three funds because of their risk rating. But I'm not satisfied this advice was suitable because of the CGT that Fidelius knew would be incurred where there was the option to manage that over the coming years. And I note that the portfolio turnover after the 2021/22 tax year trades were significantly reduced – as referred to below – and the CGT looks likely to have been more manageable. I'm not convinced that Mr A would have agreed that his overriding concern at the time was to have all his assets to be managed on a discretionary basis at the expense of such a large CGT bill but for the advice given to him by Fidelius that the investments were too high risk for him. I think overall, there was no reason that the funds couldn't have been considered as part of his total portfolio and that risk was managed.

So, I uphold this complaint point and have detailed below how the matter should be put right below.

<u>The level of trading</u>

As a result of Mr A's concerns about the CGT liability incurred, Mr A looked further into the management of his portfolio which caused him to complain about the high turnover, or 'churning' of his investments and the impact that had on his portfolio incurring costs and tax.

For completeness I include the regulator's – the Financial Conduct Authority's – definition of 'churning and swithcing' as detailed in its Conduct of Business Sourcebook ('COBS') COBS 9.3.2 G;

> (1) A series of transactions that are each suitable when viewed in isolation may be unsuitable if the recommendation or the decisions to trade are made with a frequency that is not in the best interests of the client.
>
> (2) A firm should have regard to the client's agreed investment strategy in determining the frequency of transactions. This would include, for example, the need to switch a client within or between packaged products.

It's clear that any trading must be in a firm's client's best interests and not for the benefit of the firm and has to be in line with the agreed investment strategy.

Over the years, the turnover in Mr A's portfolio was;

Tax Year	% Turnover	Total Disposal Proceeds	Total Gain Realised less CGT allowance
2017/2018	68%	£558,419.77	£40,571.75
2018/2019	51%	£822,828.03	£22,430.52
2019/2020	127%*	£474,583.13	Zero
2020/2021	113%*	£928,160.23	£39,545.03
2021/2022	3%	£44,857.80	Zero
2022/2023	0%	£234,305.16	£104,445.77**

*PAM acquired PIM and the portfolios were realigned. After that PAM's portfolio was partially structured as an OEIC within which the majority of trading was done so trading in Mr A's portfolio was significantly reduced.

**The large capital gains tax liability came about because of the sale of the three funds.

The service offered was a model portfolio and not a bespoke portfolio and as mentioned above I haven't found any reference for the need to manage CGT. Fidelius has provided sample copies of PIMS' 'Summary of Parallel Model Portfolio Changes' which provide a commentary of the changes being proposed and carried out during the relevant periods referred to. I have cross referenced those proposed changes – the sales in particular – with what trades were carried out on Mr A's portfolio and note that they tally. This suggests to me any transactions were considered and not carried out without reason.

And looking at the trading schedules on the CGT reports they are not out of line with what I would expect to see for a model portfolio where the constituents are constantly monitored or rebalanced to stay within the realms of the investment objectives of that model portfolio. And as no charges were incurred by Mr A for the trades made to keep the portfolio in line, then, I don't have concerns about the number of trades. I say this because I think the number of trades reflects the discretionary manager carrying out its discretionary mandate and as evidenced by the Summary of Parallel Model Portfolio Changes documents.

The same information isn't available from when PAM took over PIM, but as referenced in the above table I'm satisfied with the reasons given about the higher levels of turnover in order for the portfolio to be realigned. And that turnover subsequently reduced because of the OEIC structure and trades were carried out within the OEIC.

And as PIM, PAM nor Fidelius financially benefitted from those trades as no commission was paid, I'm satisfied that the motivation behind the level of trading wasn't for the financial benefit of either PIM, PAM or Fidelius. They weren't remunerated when trades were carried out and looking at the trading on the CGT reports the majority of trades were carried out on set days of the month which suggests the portfolio was being regularly realigned or rebalanced to stay within the investment objective remit and the DFM's investment changes. As examples, for the 2018/19 schedule shows 11 sales took place on 14 August 2018 and 25 on 4 September 2018. This suggests to me trading dates were set, and the portfolio rebalanced by switching holdings or tweaking the number of units held in the underlying funds and so weren't just arbitrary transactions.

Mr A has concerns that the high level of trades and resulting CGT has impacted on the performance of his portfolio. However, I can't consider performance in and itself, but I can consider whether the portfolio was mismanaged.

Provided a portfolio is invested in line with its overall objectives and disclosed risk, then it wouldn't be fair or reasonable for me to uphold the complaint on this point. I haven't seen anything to suggest that the portfolio was invested outside of its stated investment objectives or risk profile.

And the fact that the risk of underperformance of the portfolios materialised against the benchmarks, does not automatically mean that the Fidelius did anything wrong. In the absence of any evidence that Fideulius mismanaged the portfolios – and the performance of the portfolios alone doesn't evidence this – I am unable to say that Fidelius has done anything wrong in the overall management of Mr A's investments.

While I can understand why Mr A may not be happy with the performance of the portfolio during the period in question, but the issue of portfolio performance is not straightforward in that it is actively managed. This means the money is invested in specific assets of funds chosen by Mr A's DFM manager. If the portfolio in a certain period poorly performed that's because the DFM manager had taken certain decisions that hadn't paid off – at least in the period under review. That's disappointing, of course, but reflects the DFM manager exercising its judgment – which it was supposed to do. It doesn't mean the DFM manager had been negligent or failed in its duty of care. And it doesn't mean the DFM manager's decisions won't pay off over the longer term.

And as referred to above, the service offered was a model portfolio and not a bespoke portfolio where the management of capital gains tax can be a consideration. So, any CGT incurred was as a result of the DFM manager fulfilling its role to manage the portfolio in line with the investment objectives of that model portfolio. And, as mentioned above, apart from the limit to CGT of £20,000 referred to in 2013, I can't see that any other limits were placed on Fidelius for the CGT in its management of the discretionary portfolio.

It follows that I don't uphold this element of Mr A's complaint.

Putting things right

When upholding a complaint, this service tries to, as much as possible, put the investor back in the financial position they would have been in but for the unsuitable advice. In this case I have concluded that the advice to sell the three funds was unsuitable. So, to put the matter right Fidelius should;

- Repay to Mr A the CGT he paid to HMRC in relation to the sale of the three funds in May 2022. Mr A has provided this service with evidence from HMRC of the amount he paid and should furnish Fidelius with the same and the date of payment.
- Fidelius should pay 8% simple interest on that sum from the date the CGT was paid to the date of settlement for the time that Mr A was deprived of those funds.
- If the discretionary managed portfolio has outperformed the three investments sold in May 2022, as if they were still held, to the date of settlement, Fidelius can deduct that amount from the redress.
- If the discretionary managed portfolio has underperformed the three investments sold in May 2022, as if they were still held, to the date of settlement, Fidelius should add that amount from the redress.

My final decision

For the reasons given, I partially uphold Mr A's complaint about Fidelius Ltd. Fidelius Ltd should pay Mr A redress as laid out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr A to accept or reject my decision before 27 June 2025.

Catherine Langley
Ombudsman