Financial Ombudsman Service

complaint

Mr and Mrs D complain about the Meteor Senior Life Settlements Fund (a cell holding of the EEA Life Settlements Fund) in which they were advised to invest by Taylor Frost Wealth Management Limited ("the business"). It has been stated that:

- The investment was assessed as having a "medium" risk but in reality it has a "high" risk. The industry regulator has confirmed this.

- The investment was not suitable for them as they did not want to take a "high" risk.

background

The background to this complaint is outlined in my Provisional Decision issued in August 2014. A copy of this is attached and forms part of this decision.

Mr and Mrs D responded to the Provisional Decision, stating the following:

- They said they were not experienced investors, which is why they had used financial advisers over the last 40 years.

- Their risk level was assessed as low/medium and they have never accepted any high risk recommendations. The recommendation was represented to them as being safe.

- As a retired couple in their 60s, they would not have wanted to place such a substantial sum in a high risk investment.

Taylor Frost responded and did not agree with my Provisional Decision. In summary, it stated the following:

- Insufficient weight has been placed upon how the business came to view the fund as having a medium risk. Between 2008 and 2010, both Meteor Asset Management and EEA marketed this fund as having a 'low' risk and being uncorrelated to equities. This was further reinforced by Meteor's statements concerning the fund's positive returns and growth over the last four years. As such, it was entirely reasonable for an IFA to conclude that the fund was medium risk and not high risk.

- Its view of the risk categorisation of the fund was in no way disabused by the regulator. Therefore, the failure was with the regulator if it had always viewed the fund as high risk during this time.

- It was logical and good practice to rely on the letter from EEA dated 23 June 2009, which attached a statement dated 15 June 2009 explaining that EEA's accountant had verified that its policies could be sold to meet redemptions at current values. EEA also said in the statement that the accountant would check its "mark-to-model" valuations against "mark-to-market" and was comfortable that its valuation represented "at least market". It also said that lives assured in the fund on average survived for only half their remaining life expectancy.

- An investment portfolio should contain a range of different asset types with low correlation to each other as this lowers the overall risk. Educational materials from an industry examination body also stated that US life settlement policies had no correlation to equities.

- The business' due diligence had found that an insurance company in the US had never failed to meet its obligations to fully pay out on a policy. Also, the business understood that state guarantees were in place to protect policyholders if an insurance company failed.

- Since the launch of the EEA fund, there had been 57 claims totalling (US)$65m which had occurred at an average of half of the initial life expectancy of the lives assured. The policies were therefore maturing well within the fund's model.

- The Financial Services Authority (FSA) visited the business in 2007 as part of its thematic review of the life settlement sector. It would have seen recommendation letters that described the fund as medium risk and did not raise any concerns over this or state that the fund should be described as high risk.

- Mr D has said that he was not an experienced investor. However, he was a high net worth investor as he had invested over £1 million in non-pension assets over 15 years and had a pension fund of £500,000. He had also gifted sums to his children to mitigate inheritance tax. Further, in the assessment of his risk profile, he agreed with the statement about being used to taking risk and disagreed with the statement concerning a preference for deposits over stock market investments. Lastly, Mr D opted to transfer his pension to a drawdown arrangement rather than take an annuity which showed he was comfortable with taking risk.

- Mr and Mrs D held other high risk investments in 2009 as part of their portfolio and they still held these in 2012.

- The amount invested in the EEA fund was a very small proportion of their non-pension assets. The advice to invest in the fund should not be looked at in isolation and instead should be viewed as part of the wider portfolio. This also adhered to the regulator's guidance that only high net worth individuals could invest in such a fund and that this should constitute only a small proportion of their capital.

- The business had attempted to remove its clients from the fund a couple of days prior to the announcement from the FSA in November 2011. However, this was not possible as EEA subsequently suspended the fund as a result of the FSA's announcement and especially because it had described such funds as "toxic". If it was not for this announcement, Mr and Mrs D would have instead realised a gain.

- The business had previously increased Mr and Mrs D's wealth by £160,000 by placing £214,000 into Keydata structured products. Also, the business had realised a profit of £50,000 for Mr D by advising him to invest in a property fund. Further, it recommended enhanced annuity rates which continue to benefit him today and other investments that have financially benefited both Mr and Mrs D.

- The fund was repeatedly described as "low risk" in product literature. Mr and Mrs D's complaint would therefore be better directed to Meteor or EEA.

my findings

I have reconsidered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

I would firstly comment that many of the business' further submissions have already been raised previously in our investigation of the matter, and have been addressed within the provisional decision. As such, I would refer both parties to the findings set out in that attached decision, but where appropriate, and in the interests of fairness, I will comment further.

I note that the business has argued that insufficient account has been taken as to how it initially arrived at its view that the Meteor Senior Life Settlements Fund was a medium risk investment and therefore suitable for Mr and Mrs D. It has reiterated that this was because the fund had been marketed as low risk, uncorrelated to equities and having produced positive returns during the previous four years.

To add to my comments relating to this in the provisional decision, I note that the product brochure explained that such funds were relatively new to the UK but that there had been an active market in the US for several years. One of the reasons given to invest was that the returns were not linked to traditional asset classes. In essence, the fund would consist of second hand life policies which had been purchased within the US at a discount. The insurance pay-outs on these policies, following the death of the policyholders, would then be used to maintain the required premiums on the remaining policies and ultimately produce the returns to investors. All this involved several different and unconnected parties who were responsible for administering and overseeing the arrangement. As such, I believe this was an investment which could be considered less than mainstream and particularly niche.

Accordingly, the brochure set out a broad range of risks. For example, there was a risk that the returns on the fund could be less if there was a failure by the investment adviser in sourcing and pricing new policies or if the calculation for the life expectancy of the policy holder was wrong. Further, there was liquidity risk because the second hand market for life settlements was not highly regulated or developed, so there could be difficulty in selling policies and/or this would have to be done at a loss. The fund was also managed overseas and so there was the exchange rate risk and a lower level of consumer protection.

As noted previously in my provisional decision, the regulator at the time, the FSA, issued guidance about this type of fund in 2012. It stated that such funds were high risk and that these risks were opaque and largely misunderstood by both consumers and advising businesses. The regulatory guidance is still that this type of fund is a complicated investment and that "firms should not be marketing, recommending or selling these products to the mass retail market".

As stated in the provisional decision, even if the Meteor fund was described with the promotional literature as low risk, the adviser should still have taken into account the nature and operation of the fund and the range of risks inherent within it. In the provisional decision I found that Mr and Mrs D's assessment of risk was more consistent with the lower end of the "balanced" scale and perhaps leant more towards "cautious". To reiterate, they indicated a strong disagreement with being comfortable at the prospect of "*their investments falling and rising rapidly*" and strongly agreed with the statement that "*the thought of losing my money makes me nervous*". Additionally, they were strongly averse to taking "*higher risk in order to make higher gains*".

I acknowledge the business' observation that Mr D had also agreed with the statement within the risk assessment about him being accustomed to taking financial risk and that he disagreed with the statement for preferring savings accounts to stock market investments. However, it is important to note that I have not concluded that Mr and Mrs D had not invested or taken investment risk previously. Rather, it is my view that they were prepared to take some risk, but that in view of their circumstances and their expressed preferences they were inclined to significantly limit the risks they would now be taking.

I concur with the view expressed by the business that the performance of this type of investment would have been uncorrelated to other more traditional and well known investments. But that would not mean that it was therefore suitable, and for the reasons set out in the provisional decision, I do not consider that it fulfilled Mr and Mrs D's requirements or that its lack of correlation to other assets such as equities would necessarily render it suitable. Overall, on the basis of the risks already described and the nature of the investment, it is my view this was a complex and sophisticated investment which presented a significant risk to Mr and Mrs D's capital. Even taking account of the aim of diversification, for the reasons stated I do not consider it to have been appropriate to have recommended such an investment.

Although favourable past performance may have been experienced by the fund up to the point of advice and it had been described as low risk within the literature, the risks of the fund, which I have previously summarised and which were described within the promotional literature, should in my view have made a professional adviser sufficiently aware that the fund was nevertheless not appropriate for investors such as Mr and Mrs D.

As stated previously, I consider that it is the role of the adviser to look beyond the risk categorisations made within any marketing literature and commentary and take into account the nature of the fund's assets and its underlying features before making their own assessment of the suitability of the product for clients such as Mr and Mrs D. Likewise, an assessment of favourable historic fund performance can be useful, but it says little about the underlying features of the investment or its suitability for specific consumers and their objectives. Indeed, it may often be the case that reasonable fund performance masks inherent unsuitability and it is only when the performance deteriorates and losses are incurred that consumers may be alerted to such issues.

It has been reiterated by the business that if the regulator viewed the fund as higher risk in 2009 and 2010, then this should have been made public at that time and the business should not be liable for a regulatory failure. The FSA subsequently issued guidance about this type of fund in which it said they were high risk. Even though this guidance was not produced until after the investment was sold to Mr and Mrs D, it is my opinion that the regulator's view would have been that this type of fund had always presented a significant risk. The FSA said that its review had shown it likely that a high proportion of these investments were previously mis-sold, which had resulted in the guidance being issued. Importantly, it did not state that its view on such investments had recently altered.

Moreover, I do not consider it to be necessary to comment on why the FSA did not issue such guidance earlier than it did on such funds, or why concerns were not raised about this particular fund during a visit in 2007. The important fact to bear in mind is that, when the disputed investment was sold to Mr and Mrs D, the business had an obligation to consider the features of the product – not just the headline description - and ensure that it was suitable for Mr and Mrs D before making its recommendation.

The business has stated that it carried out its own due diligence to assess the risk of the plan was suitable for Mr and Mrs D and indeed I note that it appears to not have taken the "low risk" description in the fund fact sheets at face value, hence its own categorisation of the fund as "medium" risk. It said it carried out research and found that insurance companies in the US had not failed to meet their obligations and that state guarantees were in place in the event of any company default. Nevertheless, the literature for the plan listed a number of different – and in my view significant - risks and stated that if one or more of these materialised, it could have an impact on the capital return. As such, and notwithstanding the fund's risk description in the literature and its past performance, I am of the view that an analysis of the product's features and risks should have determined that it was not an appropriate investment for Mr and Mrs D.

The business has stated that it was good practice to have relied on a letter from EEA from June 2009, which included a statement from the fund's accountant. This indicated that the fund was being managed adequately on the basis of its valuations of the underlying policies and that these were maturing in line with, or prior to the predictions used within the modelling. However, whilst reassurance may have been taken from this, the future returns on the fund were nevertheless dependent on the predictions used within the modelling continuing to be accurate. Similarly, sufficient cover for redemptions would not have removed the potential for liquidity problems in the second hand policy market if these exceeded expectations, which could mean there was a risk that if policies needed to be sold this could still be at a discount to the purchase value and/or be very difficult to be sold at short notice.

In terms of Mr D's level of financial experience in particular, in his submissions to the provisional decision, Mr D has described himself as an inexperienced investor. The business has disputed this, stating that he was experienced because he held a large portfolio of non-pension investments. Furthermore, it has said that there was evidence that Mr D had taken risks before such as when he opted for pension drawdown rather than an annuity.

However, as stated in the provisional decision, whilst I am satisfied that Mr D was not necessarily an inexperienced investor, I am also of the view that he had been largely reliant on professional advice in making his investment decisions, as he was in this particular instance.

Furthermore, as also stated previously, I am not of the view that the degree of financial experience which could be attributed to Mr D or Mrs D would have enabled them to understand the degree of risk they were taking with the recommended fund, given its complexity and non-mainstream nature.

As in the provisional decision, I acknowledge that the investment of £40,000 was a relatively small part of Mr and Mrs D's overall capital. Similarly, the business has argued that this investment should not be viewed in isolation and instead should be in the context of the rest of Mr and Mrs D's portfolio. However, notwithstanding that this advice was seemingly specific to Mr D's pension lump sum, and constituted a significant part of this, I would simply reiterate my previous comment that, even if it represented a small amount of their overall assets, it remains the case that Mr and Mrs D were in the process of reducing their exposure to risk. The recommended fund was not in my view consistent with that objective and was above the level of risk which Mr and Mrs D were prepared to take.

I acknowledge the further comments relating to the FSA announcement regarding the fund and that it was suspended shortly thereafter. However, as stated in the provisional decision, I am of the view that, due to the nature of the underlying policies, the market that provided the mechanism to be able to buy and sell such policies and the complex strategies needed to maintain the fund, the potential for such liquidity problems within the fund should have been apparent to the adviser at the start. As I have said previously, this was a unique and less than mainstream investment. As such, I remain satisfied that the losses incurred by Mr and Mrs D stemmed from the original advice.

In closing, I acknowledge the business' comments that Mr and Mrs D have profited, and continue to do so, from other aspects of its advice. But for the reasons stated in this and the attached provisional decision, I remain of the view that the complaint about this particular investment should be upheld.

my final decision

My final decision is that I uphold the complaint. In resolution of the matter, Taylor Frost Wealth Management Limited should undertake the following:

fair compensation

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

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

To compensate Mr and Mrs D fairly, the business must:

compare

- the current value of Mr and Mrs D's investment;

with

- the position they would be in if 50% of their investment had produced a return matching the average return from fixed rate bonds and 50% had performed in line with the FTSE WMA Stock Market Income Total Return Index ('WMA income index') over the same period of time.

If there is a loss, the business should pay this to Mr and Mrs D. I have decided on this method of compensation because:

- Mr and Mrs D wanted growth and were prepared to accept some investment risk.
- The average rate is the rate for fixed rate bonds with 12 to 17 months maturity (as published by Bank of England). The WMA income index (formerly the APCIMS income index) is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds.
- The average rate from fixed rate bonds would be a fair measure for a consumer who wanted to achieve a reasonable return without risk to the capital invested. The

WMA income index would be a fair measure for a consumer who was prepared to take some risk to get a higher return.

- I consider that Mr and Mrs D's risk profile was in between, in the sense that they were prepared to take a degree of risk to attain their investment objectives. So, the 50/50 combination would reasonably put them into that position.
- It does not mean that Mr and Mrs D would have invested 50% of their money in a fixed rate bond and 50% in some kind of index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of return they could have obtained from investments suited to their objective and risk attitude.

how to calculate the compensation?

The compensation payable to Mr and Mrs D is the difference between the fair value and the actual value of the investment. If the actual value is greater than the fair value, no compensation is payable.

The actual value is the value Mr and Mrs D will receive if they terminated the investment on the date of my final decision.

actual value

At present it is my understanding that Mr and Mrs D cannot access the funds they invested in the Meteor Senior Life Settlements Plan. As a result, if the restriction is still in place at the date of settlement, the business should assume an actual value of nil. The business may then take ownership of the plan. Mr and Mrs D would need to agree to facilitate this transfer and any assignment or agreement of that nature, but the business must meet the cost of any such assignment. The business would be entitled to any income or capital distributed from the investment in future.

total fair value

This is what the investment would have been worth if it had obtained a return using the method of compensation set out above. It is the total of 'average rate element' and 'WMA income index element'.

average rate element

To arrive at this value the business should:

- find out the average rate for fixed rate bonds, as published by the Bank of England, for each month from the date of investment to the date of surrender;
- the rate for each month is that shown as at the end of the previous month;
- use the rate for each month to calculate the return for that month on 50% of the investment;
- the calculation should be carried out on an annually compounded basis; that is, with the return added to the investment at each anniversary;
- work out the value to the date of surrender, or to the date of this decision as appropriate.

WMA income index element

To arrive at this value the business should:

Work out what 50% of the investment would have been worth, if it had performed in line with FTSE WMA Stock Market Income Total Return index to the date of surrender, or the date of this decision as appropriate.

additional capital

Any additional sum that Mr and Mrs D paid into the investment should be added to the calculation (split equally between average rate element and WMA income index element) from the point in time when it was actually paid in so that it starts to accrue a return in the calculation from that point on.

withdrawals and income payments

Any withdrawal or income payment that Mr and Mrs D received from the investment should be deducted from the calculation (split equally between average rate element and WMA income index element) at the point it was actually paid so it ceases to accrue any return in the calculation from that point on.

If there are a large number of regular payments, to keep calculations simpler, I will accept if the business adds all those payments to the actual value and compares that total with the total fair value instead of periodically deducting them.

Philip Miller
ombudsman

Copy of Provisional Decision

complaint

Mr and Mrs D complain about the Meteor Senior Life Settlements Fund in which they were advised to invest by Taylor Frost Wealth Management Limited ("the business"). It has been stated that:

- The investment was assessed as having a "medium" risk but in reality it has a "high" risk. The industry regulator has confirmed this.
- The investment was not suitable for them as they did not want to take a "high" risk.

background

The adjudicator who considered the matter concluded that the complaint should be upheld. In summary, it was stated that the recommended fund was complex and has a significant risk of capital loss. He was not persuaded that Mr and Mrs D were prepared to accept this risk at the time. In support of this, it was noted that they were seeking a reduction in the overall risk of their portfolio and he did not consider the Meteor plan was suitable for achieving this aim.

The business has confirmed that it does not accept the adjudicator's conclusions, however, stated the following in summary:

- Mr and Mrs D were seeking an asset which was uncorrelated to equities and the recommended fund, which was also described in fund fact sheets as being "low" risk, was consistent with this.
- As it had also demonstrated strong performance over a period of relative instability, the fund was justifiably viewed as being a "medium" risk investment.
- The regulator at the time, the Financial Services Authority (FSA), allowed the product to be described as "low" risk.
- Third parties such as a prominent accountancy firm had verified that the policies within the fund could be sold to meet redemptions at current values and that the model was therefore viable.
- The product literature emphasised the stability of the plan and that it was not correlated to equities.
- The fund had been very stable, with a healthy performance record, over the four years prior to investment and so it was reasonable to say it had a "medium" risk.
- A significant amount of time was spent meeting with Mr D to discuss the investment.
- The industry regulator has only recently said that the plan has a "high" risk. The business does not consider this was the case in 2009 and that any other conclusion would be using the benefit of hindsight.
- Only Mr D attended the investment meeting, and as the investment was derived of his pension assets, he was making the investment decisions for him and Mrs D and answering questions regarding their attitude to risk.
- It was determined at the time that Mr and Mrs D were seeking a balance of low, medium and high risk investments. They had an overall "balanced" attitude to risk, and it was not nearly "cautious". This was accepted by Mr D at the time and was confirmed within the complaint submissions.
- The answers to the risk questions as cited in the adjudication had been selectively quoted and comments which contradicted a low risk attitude had been ignored.

- Mr and Mrs D stated they were uncomfortable with the prospect of their investments rising and falling, which is why an asset class with a proven track record and no correlation to equities was selected.
- Although they also stated that they were nervous about losing money and did not wish to take a higher risk, it had not been confirmed that they had in fact lost money to date.
- A holistic assessment should be undertaken of Mr and Mrs D's financial situation, as had been the case when advice was given, rather than selecting just the one investment.
- The risks associated with the investment were brought to Mr and Mrs D's attention.
- The run of on the fund was caused by the FSA's statement rather than being a result of a liquidity issue caused by the underlying investments.
- The risk of capital loss was not hidden from Mr and Mrs D. It was also the case that the APCIMS (now WMA) index which had been suggested for redress comparison purposes had also reduced significantly in 2008/09. However, no capital loss had yet been incurred within the recommended fund.
- Mr and Mrs D were not ordinary retail consumers, but experienced high net worth investors. Any other conclusion had been drawn with the benefit of hindsight. As such, the regulator's guidelines did not prevent a business from recommending such funds to them.
- Mr D was prepared to accept capital loss for the prospect of greater returns.
- Mr D was an experienced investor with a large portfolio and had established many risk bearing investments prior to this. If they didn't want to accept, or did not understand the risks associated with the fund they would not have invested.
- The attitude to risk questionnaire also demonstrated that Mr and Mrs D did not want cash based investments. The plan was sold to diversify away from equities. This was made clear to Mr and Mrs D and it was also their intention to diversify away from their assets in the pension and SIPP portfolios.
- The recommended investment constituted a relatively small proportion of their non-pension (and home) assets, being less than 5% overall. Their portfolio was well diversified, even taking account of this investment.
- It advised Mr and Mrs D to withdraw from the fund but they were unable to do so due to its suspension, which itself had been caused by regulatory intervention.

The adjudicator responded to the business, setting out in brief his opinion that it was not the regulator's opinion that the recommended fund had only recently become high risk – no time frame had been given. The regulator in fact stated that a high proportion of the investments had been mis-sold previously, which was why it was issuing guidance at that time.

It was reiterated that, in his view, the recommended fund was a complex and opaque investment which had a very significant risk of capital loss. It was accepted that Mr and Mrs D were prepared to take some risk, and that it was not necessarily disagreed that they would have been "medium" risk investors, but the responses from Mr D to the risk assessment indicated that he wished to avoid capital losses, particularly significant ones. This also appeared to be corroborated by a reduction in the overall risk exposure of the portfolio over time, facilitated by the involvement of the business.

The adjudicator further reiterated his view that Mr and Mrs D should have been informed of the higher risk of the individual investment, even though they may have sought diversification. It was also stated that they were retail investors, to whom the fund, which was an unregulated collective investment scheme (UCIS), should not have been promoted.

The business maintained its stance, however, stating the following points:

- It was clarified that Mr and Mrs D had been categorized as "balanced" risk investors rather than "medium" risk investors and it was not accepted that they were ordinary retail investors. They were regarded as high net worth investors and Mr D himself was recorded in the fact find as not being an inexperienced investor.
- Mr D also opted to enter into income drawdown in 2009 as opposed to buying a secure annuity, following a meeting and presentation on this. This was not consistent with a cautious investment approach.
- Meteor did not require a statement from Mr and Mrs D when they applied for the investment confirming that they were high net worth investors.
- Every investor aimed to avoid capital losses – however Mr and Mrs D were prepared to accept the risk of capital loss for the sake of enhanced returns. An example of the business proactively advising Mr and Mrs D in order to maintain returns and minimise losses was the recommendation that Mr and Mrs D exit from property funds in 2008.
- The evidence indicated that Mr D's attitude to risk was properly assessed and recorded.
- Life settlement funds were introduced as a way of investing in an asset which was producing higher returns than cash deposits but was uncorrelated to equity markets, which had recently been volatile.
- The fund was endorsed as being suitable for portfolio diversification in financial publications and was labelled as "low risk" by Meteor – as permitted by the regulator. Due diligence was undertaken and there was reliance upon such factors in providing the recommendation.
- The fund was therefore entirely suitable for "balanced" risk investors such as Mr and Mrs D.
- It was also reiterated that the APCIMS index, with its significant equity exposure, was an inappropriate benchmark for redress comparison purposes as this was exactly the type of asset class which Mr and Mrs D wished to avoid. Cash rates would be more appropriate.

As agreement has not been reached on the matter, it has been referred to me for review.

my provisional findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

With regard firstly to Mr and Mrs D's attitude to risk, this was assessed as "balanced" by the business. It seems that only Mr D was present at these meetings but this was seemingly usual and acceptable to them both. Mr D was recorded as being prepared *'to accept a higher level of investment risk and volatility for the potential of higher returns'.* However, it is clear that they were at the lower end of this rating and were in fact close to being categorised as "cautious" investors. I have noted the comments relating to the citation of individual answers, and acknowledge that there are responses which would indicate that Mr and Mrs D were prepared to take some risk.

However, other responses, such as strong disagreement with the prospect of "*their investments falling and rising rapidly",* strong agreement that *"the thought of losing my money makes me nervous"* and being strongly averse to taking *"higher risk in order to make higher gains"* lead me to conclude that Mr and Mrs D's score was consistent with that lower end of the "balanced" scale, and perhaps just as much with the "cautious" rating below this.

It is also worth noting that the investment report stated that that they wished to *"lean towards investment vehicles that are no more than medium risk"*. Importantly, this was not a description for a "medium" overall risk for their portfolio, but individual investment vehicles with no more than "medium" risk.

In terms of investment experience, although Mr D disagreed that his experience was very limited, neither did he strongly disagree, which was also an option. He was used to taking financial risk, which may well in any case have referred to greater previous investment in equities, but was also ambivalent on the statement relating to having sound financial knowledge to help him make investment decisions. I would also not necessarily regard individuals who had exposure to the types of investments held by Mr and Mrs D (as set out below) to have sufficient financial sophistication to be able to understand the risks involved in more complex investments, such as the Meteor plan. Therefore, whilst I would agree that Mr D may not have been an inexperienced investor, he was nevertheless not particularly experienced either and was, perhaps more pertinently, clearly reliant upon recommendations made to him by the advising business.

It is of course also the case that such scores and their categorisation are somewhat arbitrary and subjective by nature, and whilst risk 'ratings' can be helpful, it is also important to take account of the investors' circumstances and objectives.

The information recorded at the time of the recommendation showed that Mr D was semi-retired, undertaking some consultancy work, and Mrs D was fully retired. Between them, they had an annual income of approximately £220,000 and they held the following savings and investments:

- £250,000 on deposit
- A portfolio of unit linked investments with a value of around £500,000
- £170,000 in National Savings Certificates.
- £10,000 in Premium Bonds
- £190,000 in structured products

Mr D was about to release around £150,000 from his pension arrangements. In broad terms they were seeking advice on how to invest some of this money.

It is well documented that Mr and Mrs D's portfolio at an earlier time had contained investments which had a higher risk. They were clearly uncomfortable with this and had been taking steps to lower the risk of their portfolio over time. The Meteor investment was established on the basis that is it was not correlated to equities as these had been volatile in the recent past. The consumers did not want an investment that would fall in value by a great degree and this has seemingly been a consistent theme from the time of the recommendation onwards. Given that they were effectively approaching full retirement and the tax free lump sum was a "one off" event, this is not to be unexpected and I consider it reasonable to conclude that Mr and Mrs D did not want to take a significant risk with this money at this time. I therefore need to determine, without the benefit of hindsight, whether the investment fulfilled these requirements.

Following the discussion with Mr D, Mr and Mrs D were advised, amongst other things, to invest £40,000 into the Meteor Senior Life Settlements Fund. The investment report produced at the time described this fund has having a "medium" risk. A description of the plan was also provided in this document.

As both sides are aware, the industry regulator at the time, the FSA, issued guidance about this type of fund in 2012. It essentially said that they had a very high risk; the risks were opaque and largely misunderstood by both consumers and advising businesses. The current regulatory guidance is still that this type of fund is a complicated investment and that *'firms should not be marketing, recommending or selling these products to the mass retail market'.* It is also relevant to note that this fund is a UCIS and should not be marketed or recommended to ordinary retail consumers in general terms. I do, however, note the business' comments relating to Mr and Mrs D's net worth, even if their actual level of financial experience remains the subject of some debate.

I would also agree with the adjudicator's point that the regulator did not say these types of fund had only recently become high risk – it did not give a time frame about this – and there was no accompanying indication of it having changed a previously held differing view on the matter. It said that its review had shown it likely that a high proportion of these plans were mis-sold previously and this was why it was issuing guidance at that time. So I consider that it is reasonable to say that its view is that these plans always had a significant risk.

The regulatory guidance led to increased withdrawal requests from this fund. Given the illiquid nature of the assets within the fund, it could not meet these requests and it was suspended. It has not reopened in full and my understanding is that it is now in the process of being wound up. The FSA, in principle, gave information that it said should have been made clear to consumers at the time of sale. It did this because it thought that these products were being widely mis-sold and consumers were being misled about their risk.

Whilst I take the point relating to the timing of the large number of withdrawal requests, therefore, I am of the view that Mr and Mrs D's loss stems from the advice they were given to invest in an investment which had such features in the first place. I am not of the view that this was caused by the actions of the regulator or any other third party that may have issued its opinion on the risk and nature of the fund.

Whilst I must form my own view of the suitability of the advice, I have nevertheless noted the industry regulator's guidance, as outlined above. As stated by the adjudicator, the fund in which Mr and Mrs D were advised to invest has particular characteristics. It invests in the life assurance policies of US citizens. It aimed to benefit from insurance pay-outs on the death of the original policyholders. Because of the nature of the investment, complex strategies and calculations are needed to "estimate" how long people will live. However, if these calculations are wrong, then significant money could be lost or access to the investment may be restricted.

This type of fund can also have significant liquidity problems due to the nature of the underlying investments, as has happened in this instance. As they are based overseas, consumer protection can be reduced and there is the additional exchange rate risk. On "rare occasions", it was stated that policies may have to be sold, and so there was also a risk that this could be at a discount to the purchase value and/or very difficult to be sold at short notice. So overall, I consider it reasonable to conclude that the fund had a significant and material risk of capital loss.

In my consideration of the overall suitability of the plan in the context of whether it represented too high a risk for Mr and Mrs D, I have also taken into account the nature of the underlying policies themselves and the market that provided the mechanism to be able to sell and purchase such policies. This was in my view, for the reasons already stated, a somewhat less than mainstream asset class (as also confirmed in the reliance by the business on its lack of correlation with any other type of asset class) which was based overseas.

At this point, it is worth stating that, although I note that reliance has been placed upon the fund's lack of correlation with equities, I am not of the view that Mr and Mrs D necessarily had an aversion to equities per se, but were instead seeking a move away from higher risk asset classes in general. It would therefore not be appropriate to replace equities as an asset class with a product which still had significant – albeit perhaps different in some ways – risks, such as the possibility of withdrawal restrictions due to illiquidity and significant capital losses.

Therefore, I am of the view that the recommended fund represented considerable risks and would only have been suitable for very experienced retail investors. Although I note the debate regarding their actual level of financial experience, I am not of the view that this was a description which could reasonably be applied to Mr and Mrs D or that, given their objective and answers provided to the risk assessment, they would have been prepared to accept the level of risk presented by the investment.

It has been further argued that, on the basis of the documentation provided, Mr and Mrs D would have understood how the investment operated, along with the different risks. The business has also said that Mr and Mrs D were referred to the bond literature which explained the risks and it was reasonable for the business to have relied on this. I have noted that the documentation did state that the return of capital was not guaranteed and that Mr and Mrs D could receive a lower sum upon surrender. I also accept that the plan literature stated examples where the capital invested could be at risk or where there might be restrictions on withdrawals.

However, I am not persuaded that this would have enabled investors such as Mr and Mrs D to understand the degree of risk they would be taking, particularly taking account of the investment's unusual features. When considering the considerable risks inherent in the product and Mr and Mrs D's risk appetite, it is my view that the product was unsuitable for them. In any event, the business will be aware that the level of detail within the correspondence and the plan literature would not justify the recommendation of an unsuitable investment.

I appreciate that the business would consider it was entitled to rely on the literature produced by Meteor as a regulated business. However, notwithstanding this, the literature did set out a number of risks arising from the nature of the underlying life policies and the structure of the investment, including the model and the manner in which the fund would operate. I would also state that it is not sufficient for a business to simply assert that it relied on the headline description of the investment when making its assessment of suitability. Similarly, it would not be fair or reasonable for the business to rely on warnings within its investment report where the value of the investment could fluctuate or there could be a risk to capital. Rather, it should be exercising professional judgement about the inherent nature of the investment and its suitability for its clients' particular investment needs. Importantly, the business should have identified those significant risks inherent in this product and taken them into consideration when recommending the investments to Mr and Mrs D.

As such, I remain of the view the business should have been alerted as to risks of the plan and the potential peril it represented to Mr and Mrs D's needs in terms of their risk profile and their objective – as a reminder, to invest in in products that are no more than “medium” risk – in their retirement.

I note the business has argued that the fund represented a small proportion of Mr and Mrs D’s overall assets. However, even if the investment had represented less than 5% of Mr and Mrs D’s overall net wealth, this was still a substantial cash amount which represented nearly 30% of Mr D’s pension cash lump sum, especially given the likelihood that the capital would not be easily replaceable. But notwithstanding the actual amount invested, if I am to address the “diversification” argument put forward by the business, I would reiterate my previous comment regarding the likely success of a diversification strategy which simply replaces the significant risks of equities with the significant risks of a life settlements fund. Given Mr and Mrs D’s wish to move away from investments bearing such risks, I am of the view that the product presented risks over and above those which Mr and Mrs D would have been prepared to take.

If it is the case that the adviser recognised the risks but nevertheless deemed them to be appropriate when taking account of the wider diversification of the portfolio, the question I must ask is whether Mr and Mrs D, had they been fully comprehending of the risks and ramifications presented to their capital by the unusual features of the plan, would have accepted the Meteor plan as a part – even a relatively small part – of their overall assets. For the reasons stated, I am of the view that they would not.

So my overall findings are that this fund was not suitable for Mr and Mrs D as it had a higher risk than they wanted to take at the time. I am, however, nevertheless conscious of the fact that Mr and Mrs D would have been prepared to seek the potential of obtaining returns higher than those available upon deposit – albeit without the type of risk represented by the recommended investment – and as such I am satisfied that they would have taken some risk with their capital.

But I also acknowledge the business’ comments relating to the exposure to equities which would be produced by comparison with the APCIMS (now WMA) Index and that this would not have been acceptable to Mr and Mrs D at the time. The WMA income index is a combination of diversified indices of different asset classes, mainly UK equities and government bonds, but the business has stated that the actual weighting of equities at the time was 55%.

The use of the WMA index is not intended to suggest that Mr and Mrs D would have invested their money in largely equity based investment. The overall benchmark is intended to provide a proxy for an approximation of the type of risk to which Mr and Mrs D’s investment should have been exposed in the absence of definitive evidence as to an alternative strategy which would have been used.
Nevertheless, given Mr and Mrs D’s wish to move away from higher risk investments, I find the business’ comments in that regard to be persuasive and I am therefore minded to alter the redress methodology accordingly.

my provisional decision

My provisional decision is that I uphold the complaint. In resolution of the matter, Taylor Frost Wealth Management Limited should undertake the following:

fair compensation

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

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

To compensate Mr and Mrs D fairly, the business must:

compare

- the current value of Mr and Mrs D's investment;

with

- the position they would be in if 50% of their investment had produced a return matching the average return from fixed rate bonds and 50% had performed in line with the FTSE WMA Stock Market Income Total Return Index ('WMA income index') over the same period of time.

If there is a loss, the business should pay this to Mr and Mrs D.

I have decided on this method of compensation because:

- Mr and Mrs D wanted growth and were prepared to accept some investment risk.
- The average rate is the rate for fixed rate bonds with 12 to 17 months maturity (as published by Bank of England). The WMA income index (formerly the APCIMS income index) is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds.
- The average rate from fixed rate bonds would be a fair measure for a consumer who wanted to achieve a reasonable return without risk to the capital invested. The WMA income index would be a fair measure for a consumer who was prepared to take some risk to get a higher return.
- I consider that Mr and Mrs D's risk profile was in between, in the sense that they were prepared to take a degree of risk to attain their investment objectives. So, the 50/50 combination would reasonably put them into that position.
- It does not mean that Mr and Mrs D would have invested 50% of their money in a fixed rate bond and 50% in some kind of index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of return they could have obtained from investments suited to their objective and risk attitude.

how to calculate the compensation?

The compensation payable to Mr and Mrs D is the difference between the *fair value* and the *actual value* of the investment. If the *actual value* is greater than the *fair value*, no compensation is payable.

The *actual value* is the value Mr and Mrs D will receive if they terminated the investment on the date of my final decision.

actual value

At present it is my understanding that Mr and Mrs D cannot access the funds they invested in the Meteor Senior Life Settlements Plan. As a result, if the restriction is still in place at the date of settlement, the business should assume an actual value of nil. The business may then take ownership of the plan. Mr and Mrs D would need to agree to facilitate this transfer and any assignment or agreement of that nature, but the business must meet the cost of any such assignment. The business would be entitled to any income or capital distributed from the investment in future.

total fair value

This is what the investment would have been worth if it had obtained a return using the method of compensation set out above. It is the total of 'average rate element' and 'WMA income index element'.

average rate element

To arrive at this value the business should:

- find out the average rate for fixed rate bonds, as published by the Bank of England, for each month from the date of investment to the date of surrender;
- the rate for each month is that shown as at the end of the previous month;
- use the rate for each month to calculate the return for that month on 50% of the investment;
- the calculation should be carried out on an annually compounded basis; that is, with the return added to the investment at each anniversary;
- work out the value to the date of surrender, or to the date of this decision as appropriate.

WMA income index element

To arrive at this value the business should:

- Work out what 50% of the investment would have been worth, if it had performed in line with FTSE WMA Stock Market Income Total Return index to the date of surrender, or the date of this decision as appropriate.

additional capital

Any additional sum that Mr and Mrs D paid into the investment should be added to the calculation (split equally between average rate element and WMA income index element) from the point in time when it was actually paid in so that it starts to accrue a return in the calculation from that point on.

withdrawals and income payments

Any withdrawal or income payment that Mr and Mrs D received from the investment should be deducted from the calculation (split equally between average rate element and WMA income index element) at the point it was actually paid so it ceases to accrue any return in the calculation from that point on.

If there are a large number of regular payments, to keep calculations simpler, I will accept if the business adds all those payments to the *actual value* and compares that total with the *total fair value* instead of periodically deducting them.

Philip Miller
ombudsman