complaint

Mr and Mrs B are unhappy about advice they received from Pacific IFA Limited. That was to transfer their pensions into a Self-Invested Personal Pension Plan (SIPP). The funds were then used to invest in a Harlequin Property.

They would like to be compensated for their losses including the charges and fees.

Background

I issued my provisional decision on 29 April 2016. A copy of that is attached and forms part of this decision.

Mr and Mrs B accepted my findings but queried whether the redress should be paid gross, rather than net of tax. Their representative said they are both now receiving State pension. Their main reason for continuing to work part-time is their lack of additional pension provision. If they received additional benefits from an annuity and don't continue working, they would be unlikely to be taxpayers.

Pacific did not accept my provisional decision and made a detailed reply. Their points in summary were:

- It incorrectly relied on a factual finding that unregulated third parties introduced Mr and Mrs B to Pacific. They were introduced by one third party who was an appointed representative of a regulated business.

- Pacific has several concerns because my provisional decision said there was a meeting in September 2009, where Pacific discussed with Mr and Mrs B using their pensions to buy a Harlequin property. There's no evidence of a meeting then - it's when Mr and Mrs B were introduced to Pacific by fax. And Pacific's adviser wasn't authorised until 29 September 2009. Also, to say Pacific discussed the purchase of the Harlequin property is unfairly and unreasonably prejudicial. It suggests Pacific promoted or recommended the investment, which Mr and Mrs B have not alleged. Pacific advised on a SIPP wrapper only.

- Other concerns about the facts relied on are that Mr and Mrs B don't acknowledge a meeting took place in November 2009 and deny receiving the Suitability Letter discussed then. The provisional decision says nothing turns on whether the suitability letter was received. But if it wasn't, it follows no advice was provided and Mr and Mrs B proceeded on an execution-only basis. The Suitability Letter is the only evidence from the time of the advice which proves they went ahead with the investment after being advised it was high risk and they could lose all their funds.

- The provisional decision ignores all the evidence supporting Pacific's position that Mr and Mrs B would have proceeded anyway – and knew they were not receiving advice on the suitability of the Harlequin property. The ombudsman service hasn't obtained evidence from the SIPP provider which confirms Mr and Mrs B didn't want to take legal advice. Pacific questions why not.

- The provisional decision says Mr and Mrs B reserved a Harlequin property on 6 November 2009. What evidence of this has been relied on?

- The provisional decision is required to make findings of fact but doesn't.

- It doesn't say which regulation meant the business couldn't limit the scope of its advice. The provisional decision is founded on applying COBS rules – but it has mis-applied these. The logical sequence of events imagined by COBS is that the scope of service is first agreed between the adviser and client. This decides if that scope falls within the definition of *"designated investment business"* and therefore if the client best interest rule is triggered. The "know your client" and "suitability" rules mentioned in the provisional decision are qualified by reference to the nature and extent of the service to be provided. So COBS 2.1.2 – which prevents an adviser from excluding or limiting a duty – does not apply. And it follows the information-gathering duties in COBS 9.2.2 and 9.2.3 are also qualified by the nature and extent of the service agreed.

- The information available to the adviser at the 6 October 2009 meeting did not show that Mr and Mrs B would be transferring all of their pension provision and did not identify any specific details about the Harlequin property, which wasn't chosen and reserved until a month later.

- There is no factual basis to say the advice to start the SIPP to invest in Harlequin was one transaction. They took place on different dates under different contracts and between different parties. Everyone involved treated them as two separate transactions. And the business was paid for one of the transactions only.

- The provisional decision says the FSA's January 2013 alert is not new guidance. But there's no evidence that existing guidance on the issue already existed. And the alert didn't amount to guidance as it wasn't issued under the procedure set out in FSMA 2000.

- For the above reasons, it's not relevant to consider if the advice to invest in Harlequin was suitable. But regardless, the provisional decision is incorrect in assessing Mr and Mrs B's attitude to risk. The processes followed by the adviser accurately identified them as being adventurous. They signed their agreement on the relevant form. Other factors - such as their ownership of a mortgage-free second property in Spain - confirm their ability to financially bear the risks consistent with their investment objectives. The provisional decision dismisses the relevance of this investment, purchased with a mortgage on their UK home. That's neither fair nor reasonable.

- The provisional decision records the adviser explained to Mr and Mrs B they would only be able to borrow 50% of the Harlequin property's net asset value through their SIPP – and their pension funds only covered the 30% deposit. Therefore on the adviser's own explanation the contract couldn't be completed.

  But this is factually incorrect. Mr and Mrs B had other options available to make up the shortfall, such as borrowing against their UK house as they had done to purchase their Spanish property. They were aware of this and happy to proceed.

- There was no conflict of interest with Pacific IFA receiving an annual fee when it didn't advise on the Harlequin investment. The ongoing fee was for servicing the SIPP and was a fixed fee rather than a percentage of the transfer or investment value. It was not an advice fee. It would have stopped if Mr and Mrs B had ended the servicing arrangement. It was standard industry practice at the time – and Pacific's Terms of Business confirmed what it was for. So it is not logical to find there was a conflict of interest in charging this fee.

- It is therefore contradictory for the provisional decision to argue Pacific should have advised Mr and Mrs B to invest in lower risk investments. That would have meant an initial advice fee and ongoing servicing fee became payable to Pacific.

- Pacific would not have provided advice if it had been asked to consider the suitability of the investment. It would have required a lot more information than it had to be able to advise on that.

- It is inconsistent to have concluded Pacific should have advised Mr and Mrs B to invest in safer funds. This contradicts my letter of 3 March 2016, where I've said I think they would have kept their existing pensions – and where I've said elsewhere in the provisional decision that Pacific should have advised them not to invest. And no advice was sought or provided on what to do with their pensions. So to advise Mr and Mrs B to invest in safer funds would have required pension transfer advice.

- The conclusion also doesn't match Mr and Mrs B's risk preferences, while not making any finding about what that preference was. If it's suggesting the SIPP should still have been recommended to allow for lower risk funds: the decision to award compensation for SIPP and adviser fees is then contradictory.

- The provisional decision doesn't address causation, particularly in relation to the role of the SIPP trustee, which has an independent duty to act in the beneficiaries' best interests. The trustee is also regulated and falls within COBS.

- For all the reasons already given, the redress decision is therefore illogical, based on factual error and unfair and unreasonable.

- On the balance of probabilities, the evidence supports the business.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

The response to my provisional decision from Pacific's representative made a number of points. Many of those relate to findings of fact and the rules or evidence I relied upon in coming to my provisional decision. I'm not going to deal with each point individually. But, I recognise that I need to give reasons for my decision. I will do that by summarising my response to multiple points.

How was the introduction made?

Mr and Mrs B told us how they were referred to Pacific. I accept what they say about this. There were a number of different parties involved. Some of those parties were unregulated. Mr and Mrs B found out about Harlequin and were then referred to a financial adviser. They made a separate complaint to the adviser's principal. One of our adjudicators concluded the introducer was *not* acting in his capacity as an appointed representative of that regulated firm. Mr and Mrs B accepted this. If Pacific thinks other parties share liability for paying Mr and Mrs B compensation, it is free to take independent action against them.

Sequence of events and advice given

The suitability report provides advice about starting a SIPP. It refers to discussions, but doesn't say when those discussions took place. Clearly, it was before the report was issued. In my view, it is not relevant whether Mr and Mrs B received the suitability report. The report gave advice, but it explains what had been discussed. I think it is clear that any advice given in a meeting is likely to have been reflected in the report.

Was Pacific right to limit its advice?

The FSA issued an alert in January 2013 about a business model some firms had been using. It was concerned that some firms had been incorrectly interpreting the rules about giving suitable advice. This was not new guidance, or guidance at all. It was a statement by the regulator with its view about the correct interpretation of rules that had been in place since 2007. I agree with the regulator's interpretation.

Pacific operated the business model the FSA was concerned about. It tried to limit its advice to recommending a suitable SIPP. The adviser knew that the investment would be made in Harlequin. The SIPP was started before the Harlequin contract was signed So, they were not on the same date. But, clearly the only intention was to buy the Harlequin property. In my view, that was a single transaction. I think that the advice was unfairly limited to recommending a suitable SIPP.

As the advice to start the SIPP was a regulated activity the COBS rules applied. The adviser was required to act in the client's best interests; know their client and give suitable advice. The advice to start the SIPP therefore had to consider the investment to be made in the SIPP.

Was the advice suitable?

The investment in Harlequin used all of Mr and Mrs B's pension funds. That was to pay for the deposit of 30% of the purchase price. The balance of 70% was to be raised some other way, but it's not clear to me how that would be raised. Mr and Mrs B owned their own home. There was a small mortgage due to be repaid shortly. They also owned an overseas property.

The pensions were to provide Mr and Mrs B with income in retirement. Harlequin was an unregulated, offshore property development. It didn't have a track record and the income depended on the success of the venture. I think it was a very high risk investment.

Mr and Mrs B would need to borrow to complete the purchase. This was at a time when they intended to retire. They didn't have other sources of income. In my view, this was clearly a very high risk strategy and was unsuitable for Mr and Mrs B.

What should suitable advice have been?

I think that the advice should have been not to buy the property. The pensions should have been invested in funds suitable for Mr and Mrs B's circumstances.

Pacific says that if it had been required to advise on the property it wouldn't have given advice. But, it did give advice. That advice was required to be suitable. If Pacific hadn't given advice I think it follows that Mr and Mrs B would have obtained advice elsewhere.

It's possible that Mr and Mrs B would simply have left their pensions where they were. But, on balance, I think that suitable advice would have been to invest in line with their attitude to risk. I think that they would have been prepared to accept some risk with their pensions.

Causation

Mr and Mrs B weren't given suitable advice. They were told about some of the risks of investing. But, they were referred to Pacific for independent financial advice. I think that they would have taken note of the advice from an independent professional adviser.

Mr and Mrs B had bought an overseas property and used a mortgage on their home to pay for it. But, they used it for holidays and hoped to use it in their retirement. In my view, that is a very different investment from Harlequin. They were exposing their entire pension to significant risk. This was at a time when they had very limited opportunity to make up for the loss.

I think it is very unlikely that Mr and Mrs B would have ignored advice not to invest in Harlequin. They have told us they wouldn't. And, in my experience, most people do follow advice from a professional adviser.

fair compensation

Mr and Mrs B were approaching retirement. It is quite normal to reduce risk in the last years before taking pension benefits. An adviser should have taken that into account when giving advice. This was all of Mr and Mrs B's pension. I think that the advice should have been to invest for capital growth with a small risk to the funds.

My aim is to put Mr and Mrs B as close to the position they would probably now be in if they had been given suitable advice. I think they should have been advised to invest in lower risk funds as they were close to retirement.

The loss should be calculated in the way I set out in my provisional decision. We have now received details of the amounts returned from Mr and Mrs B's SIPPs in November 2015. The loss has been calculated as £77,728.72. Simple interest is to be added to that amount at a rate of 8% gross a year from 27 November 2015 to the date of payment.

A payment of £300 is also to be made to Mr and Mrs B for the distress caused by the loss of their pension funds.

my final decision

I uphold the complaint. My award is that Pacific IFA Limited should calculate the loss and pay compensation as set out in my provisional decision.

Under our rules, I'm required to ask Mr and Mrs B to accept or reject my decision before 8 August 2016.

Roy Milne
ombudsman

Copy of provisional decision

complaint

Mr and Mrs B are unhappy about advice they received from Pacific IFA Limited. That was to transfer their pensions into a Self-Invested Personal Pension Plan (SIPP). The funds were then used to invest in a Harlequin Property.

They would like to be compensated for their losses including the charges and fees.

background

In 2009, Mr and Mrs B were introduced by third parties to Harlequin – and to Pacific. An adviser with Pacific then discussed using their pensions to buy a Harlequin property. A meeting took place on 6 October 2009. Details of Mr and Mrs B's circumstances were recorded. These were:

- Mr B was self-employed earning about £27,000 a year.
- Mrs B was employed earning just over £8,000 a year.
- They owned their own home with an outstanding mortgage of about £20,000. This was due to be repaid with the next eighteen months.
- They also owned another property worth about £200,000.
- They had savings of about £5,000 and an ISA worth about £6,000.
- Mr B had two personal pensions worth about £55,000 in total.
- Mrs B had one personal pension worth about £6,000.
- Their attitude to investment risk was recorded as adventurous.

Mr and Mrs B reserved an off-plan Harlequin property on 6 November 2009. This was to be paid for using funds from existing pension plans to pay 30% of the cost. Mr and Mrs B were advised by Pacific about a SIPP which would allow them to do this. It appears the intention was to fund the rest of the cost through a mortgage from Harlequin.

A suitability report was produced by the adviser. This explained that the advice would be limited to finding a suitable SIPP. It also explained that this would be a high risk strategy. The limits on borrowing within the SIPP were explained. The SIPP could borrow 50% of the net asset value. It isn't clear how the balance of the Harlequin property was to be paid for.

Mr and Mrs B agreed to transfer all of their personal pensions into a SIPP.

The Harlequin property hasn't been built. Mr and Mrs B's investment in it has no value. Mr and Mrs B complained to Pacific about the advice they had received.

Pacific's reply said it had made it clear to Mr and Mrs B the Harlequin investment was high risk. And that a suitability report had been provided which contained risk warnings. But Pacific said it had only provided advice on a SIPP which would allow the type of investment Mr and Mrs B wanted. It had not advised on the suitability of the investment itself; or on the transfer of Mr and Mrs B's existing pensions into the SIPP.

Pacific argued that at the time of the investment, the regulator's Conduct of Business Standards (COBS) had allowed it to provide advice restricted to a suitable SIPP "wrapper" which would allow the investment of Mr and Mrs B's choice. It was only later, in 2013, that the regulator issued an alert mentioning Harlequin investments, which required advisers to consider the suitability of the investment itself.

Mr and Mrs B referred their complaint to this service. Pacific then sent us arguments for why the complaint shouldn't be upheld.

Our adjudicator thought that the rules required Pacific to ensure Mr and Mrs B had sufficient experience and knowledge to understand the risks involved. And that they were financially able to bear them. She questioned why Mr and Mrs B had been assessed as having an “Adventurous” attitude to risk – particularly as they had invested the whole of their pension provision in a single, illiquid asset. And she thought the regulator’s 2013 alert confirmed the regulator had always required the suitability of the investment to be considered when advising on a SIPP.

Pacific did not accept the adjudicator’s findings. They felt she had ignored some of their points. They said if COBS 9 applied, it had enabled them to give restricted advice. But their position was that COBS 9 did not apply to Mr and Mrs B’s case. That section of the rules assumed the investment to be recommended was an actual investment. But they had only given Mr and Mrs B a recommendation for an investment product wrapper.

Pacific also argued that Mr and Mrs B would have lost a £1,000 reservation fee if they had not gone ahead with the Harlequin investment. The adjudicator had been quick to dismiss Mr and Mrs B’s ownership of a Spanish holiday home as confirmation of an adventurous attitude to risk – even though this had been bought off-plan before construction was complete. And we’d accepted at face value Mr and Mrs B’s position that they hadn’t received a copy of the Suitability Letter. But the fact they had completed SIPP application forms was evidence of their acceptance of the Suitability Letter contents, which had been discussed with them.

Mr and Mrs B’s complaint could not be resolved by the adjudicator. So, it was referred to me to review.

I wrote to Pacific explaining that I agreed with the adjudicator’s conclusions and intended to provide detailed comments in a final decision. But first I was revising the suggested redress to include:

- £300 compensation for distress and inconvenience
- That if Pacific couldn’t buy Mr and Mrs B’s Harlequin investment, it would need to pay future SIPP fees until the SIPP could be cancelled.

I gave Pacific time to reply. They said I hadn’t addressed a number of specific issues. They also questioned why Mr and Mrs B or the SIPP trustee hadn’t terminated the Harlequin contract and closed the SIPP to mitigate the loss of further SIPP charges.

Mr and Mrs B closed their SIPP at the end of 2015. The funds remaining in the SIPP paid out approximately £3,000 after the deduction of outstanding administration fees. To close their SIPP, Mr and Mrs B agreed to waive any right to sue Harlequin.

my provisional findings

I’ve considered all the available evidence and arguments to decide what’s fair and reasonable in the circumstances of this complaint.

Was Pacific right to limit its advice to the SIPP?

Pacific was required to know its client and give suitable advice. It was also required to act in its client’s best interests. In my view, it could not avoid that duty by unfairly limiting the scope of its advice.

Advising on a personal pension is a regulated activity. A SIPP is a personal pension. Pacific argues that the SIPP was simply the wrapper and that it was not engaged to advise on the investment. I don’t agree. This was exactly the situation the regulator was referring to in its alert of January 2013. That was not new guidance. It simply explained that when advising on a SIPP the advice had to consider the underlying investment. There is no real risk by starting a SIPP. It can be more expensive than other pensions, but the risk is with the investment.

It's clear that Pacific knew where the investment would be made. It has arranged SIPPs for a large number of clients. It was operating exactly the business model referred to by the regulator. In my view, the advice to start the SIPP to invest in Harlequin was one transaction. The advice therefore had to consider the investment.

Was the investment in Harlequin suitable for Mr and Mrs B?

Mr and Mrs B were introduced to Pacific by unregulated firms. This was with the intention of buying a Harlequin property. To do this, it had been suggested they use their pensions. But, this was all of their pension provision. In my view, that made it a risky transaction for them.

It is not in dispute that investing in Harlequin was very high risk. This was an unregulated investment in overseas property development. The income and profits relied on the successful building and completion of the development and running the hotel. I think that exposed investors to significant risks, including the possibility of losing all of their investment.

Mr and Mrs B were assessed as having an adventurous attitude to risk. They were asked a number of questions to arrive at this answer. It isn't clear to me how the answers led to the conclusion that they were adventurous. That conclusion isn't consistent with their financial position. They had virtually repaid their mortgage with limited savings. The pensions had been invested in managed type funds. The only investment exposing them to any significant risk was the second property.

Mr and Mrs B's representative has explained that the property was bought as a holiday home. It was bought off plan. It is their property with no mortgage. They raised the funds by using a mortgage on their UK property. They intend to use it in their retirement.

I accept that the second property exposed Mr and Mrs B to some risk. But, I think this was a different type of risk to Harlequin. It was something that they would own outright. It was intended as a holiday home and to use in retirement. It is not intended to be a commercial venture to produce income.

In my view, the assessment of Mr and Mrs B's attitude to risk as adventurous is not consistent with their circumstances. They were prepared to take some risk. But, they were only five years from retirement. The Harlequin investment was clearly not suitable. This is something that should have been obvious to the adviser.

There is an additional point about completing the purchase of the Harlequin property. The pension paid for the deposit on the Harlequin contract. That was for 30% of the purchase price. The remaining 70% was intended to be paid for by a loan from Harlequin. There is a dispute about exactly how that was to be paid. But, the adviser explained the limits on borrowing within a SIPP. The loan could only be for 50% of the net asset value. So, on the adviser's own explanation the contract could not be completed.

Pacific was to be paid a fee for setting up the SIPP of £2,700. It also charged a fee of £750 a year to be paid from the SIPP. It isn't clear to me what the annual fee was for. As the investment was to be made in Harlequin there would be no need for ongoing advice. And Pacific had made it clear that it was not giving advice on the investments. These fees would not have been paid if the SIPP had not been arranged. I think that is a clear conflict of interest.

What should Pacific have done?

I think it's clear that the advice should have been not to transfer to the SIPP or invest in Harlequin. This was all of Mr and Mrs B's pension provision. They intended to retire in about five years. They should have been advised to invest in safer funds in the last years before they retired.

Would Mr and Mrs B have followed suitable advice?

Mr and Mrs B discussed the investment in Harlequin with Pacific's adviser in September 2009. They then met with the adviser on 6 October 2009. A meeting then took place in November 2009 and a suitability report dated 11 November 2009 has been provided. Pacific says that the adviser's normal practice was to discuss the report. I don't think anything turns on whether the report was received.

In my view, it should have been apparent to the adviser by the meeting in October 2009 that Mr and Mrs B should not invest in Harlequin. All of the information indicates this would be all of their pension. And it was in a high risk overseas investment. I think the adviser should have advised them not to invest at that meeting.

Mr and Mrs B had bought an overseas property. But, this was to be used as a holiday home. It was not an investment. Harlequin was intended to provide some income in retirement. I think that if Mr and Mrs B had been advised not to invest that they would not have done so. And that means they would not have paid the reservation fee.

I think that the loss of their pension funds has caused some distress and inconvenience to Mr and Mrs B. This has been made worse because they are so close to retirement. In my view, that has been caused by the actions of Pacific. I therefore intend to award £300 to compensate for this.

Mr and Mrs B's representative has asked about the repayment of fees they paid to make their claim. Although they stopped using that firm they had to pay £600. Our normal approach about the payment of fees is that consumers do not need to be represented. It is therefore unusual to make an award for the payment of fees. I don't think there was any need to pay to be represented. So, I don't think I should make an award for those fees in this case.

fair compensation

My aim is to put Mr and Mrs B as close to the position they would probably now be in if they had been given suitable advice. I think they should have been advised to invest in lower risk funds as they were close to retirement.

The Harlequin contract has been cancelled and the SIPP closed. As Mr and Mrs B don't have pension plans, the compensation should be paid to them.

I think Mr and Mrs B would have invested differently. It's not possible to say *precisely* what they would have done. But I'm satisfied that what I have set out below is fair and reasonable given their circumstances and objectives when they invested.

what should Pacific do?

To compensate Mr and Mrs B fairly, Pacific must:

- Compare the performance of Mr and Mrs B's investment with that of the benchmark shown below. Pay 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.

  Pacific should also pay interest as set out below.

  If there is any loss, Pacific should pay this directly to Mr and Mrs B – but reduced to *notionally* allow for income tax. This is because if it had been possible to pay into their SIPP, this would have provided a taxable income.

  The *notional* allowance should be calculated using Mr and Mrs B's marginal rate of tax in retirement.

For example, if Mr and Mrs B are likely to be basic rate taxpayers in retirement, the *notional* allowance would equate to a reduction in the total amount equivalent to the current basic rate of tax. However, if they would have been able to take a tax free lump sum, the *notional* allowance should be applied to 75% of the total amount.

- Pay Mr and Mrs B £300 for the distress and inconvenience caused by the loss of their pension funds.

Income tax may be payable on any interest awarded.

investment name	status	benchmark	from ("start date")	to ("end date")	additional interest
SIPP	surrendered	for half the investment: FTSE WMA Stock Market Income Total Return Index; for the other half: average rate from fixed rate bonds	date of investment	date surrendered	8% simple a year on any loss from the end date to the date of payment

actual value

This means the actual amount paid from the investment at the end date.

fair value

This is what the investment would have been worth at the end date had it produced a return using the benchmark.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, Pacific should use the monthly average rate for the fixed rate bonds with 12 to 17 months maturity 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.

why is this remedy suitable?

I have chosen this method of compensation because:

- Mr and Mrs B wanted capital growth with a small risk to their capital.

- 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 capital.

- The WMA 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 who was prepared to take some risk to get a higher return.

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

- The additional interest is for being deprived of the use of any compensation since the end date.

We have calculated the loss on the basis set out above. It assumes that Mr and Mrs B received £3,000 when the SIPP was closed. The loss was therefore £77,324.76. Interest has been added to bring the figure up to £79,336.09. That calculation will need to be updated.

my provisional decision

I uphold the complaint. My provisional decision is that Pacific IFA Limited should pay the amount calculated as set out above.