Financial Ombudsman Service

complaint

Mr G complained he was given unsuitable advice by Pacific IFA Limited ("Pacific") to transfer his personal pension plans (PPPs) to a self-invested personal pension (SIPP). The SIPP was set up to allow Mr G to invest in a Harlequin off-plan hotel development in the Caribbean ("the property").

background

In September 2010 Mr G was introduced to the investment by an unregulated representative of Harlequin. Shortly thereafter a £1,000 reservation fee was paid on Mr G's behalf. In October 2010 Mr G was referred to Pacific, and a financial review was carried out. It recorded Mr G:

- Was 50 years of age, with three non-dependent children.
- A self-employed tradesman earning £15,000 a year.
- Had two pension plans worth about £50,000.
- Had £1,000 in cash, with no other savings or investments.
- Had *about as much understanding/knowledge as the next person* when it came to investment experience.
- His attitude to investment risk wasn't recorded.

Neither party has a copy of the report giving advice. The file contains a client declaration stating the advice about the overseas room was not given by Pacific.

The transfers proceeded into the new SIPP and £30,000 was invested into Harlequin. This represented 30% of the purchase price. The remainder would be due in instalments as the property was built.

Mr G's representative complained. The final response letter said in summary that Mr G was introduced by another third party who was an introducer for Harlequin. He wanted to set up a SIPP and Pacific didn't receive any form of introduction for the purchase of the Harlequin property. Prior to the meeting with the adviser a £1,000 reservation fee was paid to Harlequin on Mr G's behalf. The COBS rules at the time didn't require IFAs to advise customers on the suitability of investments to be made by their SIPPs when making limited personal recommendations. The FSA alert was issued three years after the recommendation was made and had no formal regulatory status.

Mr G has said he was introduced to the investment by another third party. That third party paid the £1,000 deposit. He never had a face-to-face meeting with the business adviser. He telephoned him a few times and told him that it was a good investment. He didn't recall signing the declaration.

As part of the investigation, the adjudicator established that the plans that were transferred contained guaranteed annuity rated (GARs). She upheld the complaint. The COBS rules required the business to take reasonable steps to ensure that the advice was suitable, taking account of Mr G's knowledge and experience, financial situation and investment. She didn't consider limited advice was appropriate. She considered the regulator's alert was confirmation of the regulator's view on the rules. Overall, she didn't consider that Pacific could advise on the transfer to a SIPP without taking account of the intended investment. The redress suggested was based on the loss of GAR.

Pacific didn't agree with the adjudicator and said:

- The client confirmed the scope of the advice and that this was limited to the advice about the SIPP.
- The COBS rules only refer to the specific transaction and the advice given was only in regards to the SIPP. The regulator's alert didn't address this issue. They weren't providing advice on the suitability of the Harlequin investment.
- Mr G was made aware of the risks and that he could lose all of his money – but he still went ahead with the investment.
- In February and May 2015, Mr G withdrew some tax free cash and income from the SIPP. Therefore, he isn't reliant on advice from Pacific. He was comfortable managing his own SIPP without any advice. It is also wrong to assume he would buy an annuity.

Mr G confirmed he had taken some funds, as he needed the money to pay bills. He didn't – and wouldn't – seek advice again as last time it cost him dearly. He didn't remember having a meeting with the adviser.

The adjudicator answered the points raised by Pacific. She agreed that as Mr G had taken benefits the suggested redress wasn't correct as the GARs only applied at the normal retirement age of the plan. She suggested a different method of redress but still thought the complaint should be upheld.

Pacific still disagreed. Its representatives made, in summary, the following points:

- The COBS 9.2 rule refers to the "specific transaction to be recommended" – in this case the specific SIPP product to be recommended. It wasn't the investment in Harlequin property, because no advice was sought on it. The "risks involved in the transaction" relate to taking out the SIPP. These were low risks because the SIPP provider and the product itself were highly reputable.
- The reference to the financial situation refers to the current situation, not future financial situation. Clearly, therefore, this doesn't require an assessment of the suitability of the property.
- In her first assessment, the adjudicator used the words "investment objectives". This was omitted in her revised assessment. It expects that this is because the information on "investment objectives" to be obtained under COBS 9.2.2(2) is all about the "specific transaction to be recommended".
- The adjudicator refers to the FSA's January 2013 Alert, but this had no regulatory status.
- The advice wasn't to transfer the PPP; it was only about the setting up of the SIPP.
- The evidence records Mr G having already signed the Harlequin Purchase contract and proceeding without advice. He did so despite being provided with risk warnings by both Pacific IFA and the SIPP provider. Therefore, it is more likely than not that Mr G would've proceeded in any event.
- Mr G had now admitted that he took pension benefits without taking advice. Pacific felt this further supported its position. It said that Mr G tried to explain this by saying that the previous advice had cost him dearly. But of course, what has cost him dearly was his investment in a Harlequin property. He knew when he invested in that property that he hadn't taken or received advice on it, because he signed various risk warnings and acknowledgements confirming this. So at no stage had he in fact relied on Pacific IFA's advice when making the decision to invest in a Harlequin Property.

- Pacific considered the issues of contributory negligence on the part of Mr G should be taken into account. He went ahead despite repeated risk warnings. His negligence contributed to the loss suffered and this should be reflected by a lower apportionment of any redress to Pacific IFA's actions or omissions.

Mr G's representative said Mr G told them if he had been advised not to proceed he would have abandoned the whole process

The adjudicator shared additional points about the specific redress issues with Harlequin and the contract within the SIPP.

Pacific replied and said in summary:

- The SIPP trustees are under an independent legal obligation to act in the best interests of the SIPP trust at all times. If Harlequin Properties is in breach of the purchase contract between the SIPP trustee and it, then the SIPP trustees are under a legal obligation not only to act in the best interests of the SIPP trust but also to take reasonable steps to mitigate losses to the SIPP. This means they should have actively considered whether to terminate the Harlequin contract for breach, and to wind up the SIPP to prevent further SIPP fees. These steps are out of the control of Pacific and it shouldn't be liable for any future loss.
- Any direction to pay future SIPP fees, where the SIPP remains active is inconsistent with the approach to compensation awards. The actual potential loss suffered by the customer is not the entirety of the SIPP fees, but the difference between the SIPP fees and the fees the investor would've had to pay if in the ceding scheme (on a no transfer basis) or an alternative suitable pension scheme (if a transfer would still have gone ahead). No pension scheme is free. It is therefore the fee differential that represents the potential loss. This loss should also be netted down.

my findings

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. In doing so, I agree with the adjudicator. I think Pacific have done something wrong.

Mr G was referred to Pacific for advice about a SIPP for the sole purpose of investing in Harlequin. The agent for Harlequin had already sold the idea to Mr G. That agent was not regulated. The referral to Pacific was made to provide advice about the SIPP. That was a regulated activity.

There's no evidence Mr G was an experienced or sophisticated investor. Pacific knew that the investment was to be made in Harlequin. This was an unregulated, high risk, highly illiquid overseas property. There's no record of Pacific assessing Mr G's attitude to risk.

Mr G was proposing to use most of his pension savings for the deposit on an off-plan hotel room in the Caribbean. It's clear from his circumstances that he didn't have the capacity to take this risk.

Unfortunately, neither party was able to produce the suitability report. But given the annual charges in the SIPP were significantly higher than the PPPs, and taking into account the high risk nature of the property underlying the SIPP, I think the advice to transfer was unsuitable.

Pacific and its representatives put forward a number of arguments in defence of its advice. I've summarised what I consider to be the key points below, and explain why I don't agree with Pacific.

1. *Mr G only wanted advice from Pacific about an appropriate SIPP to hold the property*

Pacific said that the scope of their agreement restricted its advice to just choosing the right SIPP. It said that Mr G didn't at any stage seek or want advice on his proposed pension transfer. This is what Mr G wanted as he had already committed to investing in Harlequin and he knew Pacific was only advising on this. It said the decision on the risk of the investment was his alone and it warned him it was high risk.

COBS 2.1.1R required Pacific to act *"honestly, fairly and professionally in accordance with the best interests of its client."* This is an independent duty on the firm. It can't simply say that the customer had already decided what he wanted to do, so it simply carried out his wishes regardless of whether it was in Mr G's best interests. I'm also mindful of the principles for business and in particular principles 1 (*integrity*), 2 (*due skill, care and diligence*), 6 (*customers interests*) and 9 (*reasonable care)*.

Pacific referred to the suitability report dated 21 November 2010, in which it said it gave appropriate risk warnings. Since the report was mislaid, I've not been able to consider its contents. But I don't think it matters here – because the mere inclusion of generic risk warnings don't, in my opinion, change the responsibility Pacific had to Mr G.

I have seen a number of cases where clients referred to Pacific received limited advice. These were all cases where an investment was to be made in Harlequin. This leads me to the conclusion that it was Pacific that shows to limit the scope of its advice to simply identifying a SIPP.

And I find Pacific somewhat contradicts itself in the argument. It says it gave Mr G risk warnings about the proposed investment – showing it clearly had made some assessment about what the risks involved were.

I don't think the fact that it drew this to Mr G's attention meant Mr G was sufficiently informed of what he was investing in. This is on the basis that Pacific didn't provide evidence that it assessed Mr G's attitude to risk, or any further explanation as to what the risk warning meant and how it applied to Mr G's investment objectives.

2. *COBS 9.2 didn't apply*

COBS 9.2.1 required Pacific to obtain the necessary information about the client's knowledge and experience relevant to the specific type of *designated investment* and the investment objectives. Having done so, COBS 9.2.2 required Pacific to consider whether the transfer from the personal pension to the SIPP met Mr G's investment objectives, he could bear the risks involved, and that he understood the risks.

Pacific said it didn't have to do this for the investment. It said as the *"designated investment"* was the SIPP wrapper - that's all it had to consider. It said COBS 9.2 therefore didn't create an obligation to advise on the investment.

I don't accept this. Mr G was looking at transferring his personal pensions to a SIPP. To determine whether that was suitable or not required Pacific to understand what the SIPP was going to invest in. Pacific knew that was the objective behind the transfer. To be able to advise in accordance with the rules it had to understand the risks associated with the property. Without this information it could not say whether the transfer was suitable or not. The terms *"nature and extent of the service provided"* and *"relevant to the specific type of designated investment"* don't mean that Pacific were limited to just the choice of SIPP.

GEN 2.2.1 states "*every provision in the Handbook must be interpreted in the light of its purpose."* The purpose of COBS 9 is to ensure consumers get advice that's suitable in their circumstances. It can't be right for Pacific to interpret *'the nature and extent of the service provided'* under COBS 9.2.2 in the narrow way they propose. This would avoid looking at all of the factors that the rule (and the rest of Chapter 9) says are necessary to ensure suitability. It would defeat the *purpose* of the rule.

The interpretation applied by Pacific is too narrow, overly literal and fails to consider the regulations in context. I don't think their interpretation can be considered fair and reasonable. While the FSA Alert referred to by the adjudicator was issued in 2013, it represented a summary by the regulator of the same rules that applied in 2010. This supports this understanding of the scope of COBS 9.2. Pacific has said that the adjudicator retrospectively applied the alert to this complaint. I don't agree, for the reason given above.

Pacific argues that COBS 9.6.2 would've prevented it from giving advice beyond that of the limited scope it says it had, because Mr G didn't – and wouldn't – provide details of his wider financial circumstances. If this was the case, a prudent adviser shouldn't have made a recommendation at all – be it on an investment vehicle or the underlying assets.

3. *Mr G would have invested regardless – he didn't rely on Pacific's advice*

While looking back it's difficult to be sure what someone would have done if suitable advice had been given. Mr G has told us that had Pacific told him that the transfer was unsuitable, he wouldn't have gone ahead. Pacific said there is plenty of evidence that Mr G would have invested – but I don't agree.

Pacific was a regulated independent financial adviser. I think any advice that the transfer wasn't suitable due to the high risk nature of the underlying investment would have been significant for Mr G and carried due weight - despite what Harlequin's agent may have told him about the property. I've already explained why I think Pacific should have considered the transfer of the PPPs and the suitability of investing in Harlequin. Crucially, Pacific didn't advise Mr G *not* to transfer. It recommended the SIPP for him. He relied on their endorsement of the proposed pension transfer to facilitate the investment.

Mr G had nothing to lose by not going ahead. The £1,000 reservation fee was paid by the introducer, because Mr G was unable to afford it. That in itself should have given Pacific's adviser cause to reflect on whether his recommendation would be suitable. There doesn't seem to have been any other reason put forward for transferring to the SIPP other than to invest in the property.

I have reached this decision on the balance of probabilities. Given the significant risks involved in investing in the property, and the greater weight Pacific's advice should reasonably have had, I'm satisfied this test has been met. On balance, I think Mr G wouldn't have invested in the property had it not been for the restricted advice Pacific gave him.

4. *Responsibility of the SIPP trustees*

Pacific said that the SIPP trustees accepted the property into the SIPP, meaning Pacific can't be liable for any losses suffered by Mr G. The Trustees didn't advise Mr G to invest in Harlequin - that was Pacific's responsibility. Even if Pacific is right about the obligation on the SIPP trustees, I don't see that that the chain of causation relating to their advice and the consequences of it was broken. If Pacific feel that other parties may also be liable for the losses suffered, then that's a matter for them. Mr G contracted with Pacific. Because of Pacific's regulated advice he transferred into the SIPP and invested in Harlequin.

5. *Should an award be made to cover future SIPP fees?*

The adjudicator recommended that Mr G be compensated for ongoing SIPP fees. Pacific didn't agree it should be liable to pay future fees in full. This is because every pension plan carries fees, so any award for those fees should only be for additional fees Mr G will pay compared to the fees in his PPP. It also said that if this service was to award a lump sum in respect of future SIPP fees, the award would need to be discounted to net present value to reflect the accelerated receipt of that aspect of the loss being compensated.

Mr G has a SIPP for which he is paying charges. The only investment in the SIPP is the Harlequin property. If Pacific had given suitable advice Mr G would not have the SIPP. I therefore need to consider how Mr G should be compensated for his losses. Ideally, I would like the Harlequin property to be removed from the SIPP. And the way I intend for that to happen is for Pacific to take ownership of the property. That would enable Mr G to cancel the SIPP and avoid those future charges. But, there are difficulties with transferring the ownership. If the ownership cannot be transferred I think an award ought to be made for the additional fees Mr G will have to pay.

I accept that Mr G would have still paid fees for his existing pension. And providing a lump sum now means that Mr G will have the money available to invest or obtain a return. So possibly the lump sum should be discounted. But I don't know how long Mr G will have to pay the fees. The problems with Harlequin have been going on for some years. It isn't clear to me how much longer these problems will continue. And fair compensation should mean that Mr G will not have to pay any additional fees. But I need to compensate Mr G for his losses now.

In my view, awarding a lump sum for an amount equivalent to five years fees strikes a fair balance. It's possible that the Harlequin investment could be removed from the SIPP in less than five years. But given the time it has taken to date I think it is possible that it could take a number of years to resolve all of the issues. So using a figure of five years worth of fees is an approximate award to resolve the issue now.

For the reasons above, my view is that the transfer of Mr G's pension plans to the SIPP to invest in the Harlequin wasn't suitable. I don't think Pacific gave him suitable advice and Mr G should be compensated for this.

fair compensation

On 27 April 2016, the adjudicator contacted all parties and explained how redress in this complaint might be approached. This included certain aspects that weren't set out in the original adjudicator's view.

My aim is to return Mr G to the position that he would now be in if he'd received suitable advice. It's not easy to say what that position would have been. But I think it's likely that Mr G wouldn't have transferred his pension plans into the SIPP, wouldn't have invested in Harlequin and as a result wouldn't have opened the SIPP (and now be subject to ongoing SIPP fees). Mr G did take benefits from the SIPP. That was to pay some bills. So, I will assume that if he had kept his PPPs he would also have taken benefits at the same date. In setting out how to calculate fair compensation my objective is to address these issues. That is what I'm trying to achieve.

There are a number of possibilities and unknown factors in making an award. While we understand Harlequin will allow the business to take over the investment from the consumer. The involvement of third parties - the SIPP provider and Harlequin – mean much of this is beyond this service or the business's control.

All the variables are unknown and each may have an impact on the extent of any award this service may make. The facts suggest it's unlikely that the property will be completed and unlikely that the contract and any future payments would be enforceable. While it's complicated to put the consumer back in the position they would have been in if suitable advice had been given, I think it's fair that Mr G is compensated now. I don't think we should wait and determine each any every possibility before making an award. What is set out below is a fair way of achieving this.

I have explained how Pacific should carry this out in further detail below.

1. Obtain the notional transfer value of Mr G's previous pension plans on the date of decision if they had not been transferred to the SIPP.

The calculation should assume that Mr G would have taken action to take his benefits at the same date he took benefits from the SIPP. Pacific should assume that any contributions or withdrawals that have been made would still have been made, and on the same dates.

If there are any difficulties in obtaining a notional valuation then the FTSE WMA Stock Market Income Total Return Index should be used. That is a reasonable proxy for the type of return that could have been achieved if suitable funds had been chosen.

2. Obtain the actual transfer value of Mr G's SIPP on the date of decision, including any outstanding charges.

This should be confirmed by the SIPP provider. The difference between 1 and 2 is the loss to the pension.

3. Pay a commercial value to buy Mr G's Harlequin investment.

The SIPP only exists because of the investment in Harlequin. In order for the SIPP to be closed and further SIPP fees to be prevented, the Harlequin investment needs to be removed from the SIPP. We understand this can be done.

The valuation of the Harlequin investment may prove difficult, as there is no market for it. To calculate the compensation, Pacific should agree an amount with the SIPP provider as a commercial value, and then pay the sum agreed plus any costs and take ownership of the investment. If Pacific is unable to buy the investment, it should give it a nil value for the purposes of calculating compensation.

The SIPP has paid a deposit under a contract with Harlequin. That is the loss I'm trying to redress. Mr G has agreed for the SIPP to pay the remainder of the purchase price under that contract. Those sums haven't yet been paid, so no further loss has been suffered. However, if the property is completed, Harlequin could require those payments to be made. I think this is unlikely and as a result I think it's unlikely there will be further loss. But there might be.

Mr G needs to understand this, and that he won't be able to bring a further complaint to us if this contract is called upon. Equally, if Pacific takes over the contract from the SIPP trustees then it may be liable for the remaining amount of the purchase price. As a result any total award that Pacific may have to pay could exceed £150,000. This won't be known until the redress in steps 1 and 2 above has been calculated. If it will exceed £150,000 then this service can't tell Pacific to take over the contract from Mr G's SIPP. But we can address the ongoing SIPP fees that may continue if the SIPP can't be closed. I have dealt with this in step 5 below.

4. Pay an amount into Mr G's SIPP so that the transfer value is increased to equal the value calculated in (1). This payment should take account of any available tax relief and the effect of charges.

If it's not possible to pay the compensation into the SIPP, Pacific should pay it as a cash sum to Mr G. I note that Mr G has taken some benefits.

So had it been possible to pay the compensation into the plan, it would have provided a taxable income. Therefore the total amount should be reduced to notionally allow for any income tax that would otherwise have been paid.

The notional allowance should be calculated using Mr G's marginal rate of tax in retirement. For example, if Mr G is likely to be a basic rate taxpayer in retirement, the notional allowance would equate to a reduction in the total amount equivalent to the current basic rate of tax. However, if Mr G would have been able to take a tax free lump sum, the notional allowance should be applied to 75% of the total amount.

Simple interest should be added at the rate of 8% a year from the date of decision until the date of payment. Income tax may be payable on this interest.

5. Pay five years' worth of future fees owed by Mr G to the SIPP.

Had Pacific given suitable advice I don't think there would be a SIPP. It's not fair that Mr G continues to pay the annual SIPP fees if it can't be closed.

I think Pacific should be able to take over the investment to allow the SIPP to be closed. This is the fairest way of putting Mr G back in the position he would have been in. But I don't know how long that will take. Third parties are involved and we don't have the power to tell them what to do. To provide certainty to all parties, I think it's fair that Pacific pays Mr G an upfront lump sum equivalent to five years' worth of SIPP fees (calculated using the previous year's fees). This should provide a reasonable period for the parties to arrange for the SIPP to be closed. There are a number of ways they may want to seek to achieve that. It will also provide Mr G with some confidence that he will not be subject to further fees.

In return for that, Pacific may ask Mr G to provide an undertaking to account to it for the net amount of any payment he may receive from the Harlequin investment in that five year period up to the amount of compensation paid. That undertaking should allow for the effect of any tax and charges on the amount he may receive from the investment. Pacific will need to meet any costs in drawing up the undertaking. If Pacific asks Mr G to provide an undertaking, payment of the compensation awarded by this decision may be dependent upon provision of that undertaking.

If, at the end of those five years, Pacific wants to keep the SIPP open, and wants to maintain an undertaking for any future payments under the Harlequin investment; it must agree to pay any further future SIPP fees. If the business fails to pay the SIPP fees, Mr G always has the option of trying to cancel the Harlequin contract to enable the SIPP to be closed at any time.

6. Pay Mr G £300 for the trouble and upset caused.

Mr G has been caused some distress by the loss of his pension benefits and the uncertainty around his future benefits in retirement. I think a payment of £300 is appropriate to compensate for that.

my final decision

Where I uphold a complaint, I can make a money award that a firm pays compensation of up to £150,000; plus any interest and/or costs. If I consider that fair compensation is more than £150,000, I may recommend the firm pays the balance.

I uphold the complaint. I consider that fair compensation should be calculated as set out above. My decision is that Pacific IFA Limited should pay Mr G the amount produced by that calculation. That is up to a maximum of £150,000.

Simple interest should be added to my award at the rate of 8% gross a year from the date of this decision until the date of payment. Tax may be due on this interest.

If fair compensation exceeds £150,000, I recommend that Pacific pays Mr G the balance. And that it pays simple interest at 8% a year on the balance from the date of this decision until the date of payment.

This recommendation is not part of my award. It does not bind Pacific. It is unlikely that Mr G can accept my decision and go to court to ask for the balance. Mr G may want to get independent legal advice before deciding whether to accept this decision.

Under our rules, I’m required to ask Mr G to accept or reject my decision before 18 July 2016.

Roy Milne
ombudsman