DRN-4541219

## The complaint

Ms M complains that Morton Hill Limited, trading as McKnight Financial (MF), provided unsuitable advice to move her cash ISA into a stocks and shares ISA invested within funds that she believes were too high risk.

Ms M is concerned that her investment has gone down in value and would now like MF to recompense her for the losses that she's suffered.

Note - Ms M has also raised a complaint about the advice that she received from MF to switch her pension. I shall also address that complaint, but under separate cover.

## What happened

In June 2021, Ms M met with an adviser from MF to discuss her investment planning needs. During the meeting, the adviser completed a fact-find document with Ms M to gain an understanding of her circumstances, assessed her attitude towards risk and subsequently issued a suitability letter the following month, setting out his recommendations to her.

MF's suitability letter explained that Ms M was unhappy with the low rate of interest she was receiving on her cash ISA and as such, she wished to switch the monies to a stocks and shares ISA in order to potentially generate a better return. MF's letter went on to explain that she was content to leave the monies invested for the medium to long term, had an attitude towards risk of 'six – high medium' and had the capacity to take risks at that level. MF went on to recommend that Ms M move the £34,207 that she held in her cash ISA into an AJ Bell stocks and shares ISA, containing four different funds which they explained were in line with the agreed attitude to risk. This was in addition to the pension recommendations that MF made to both Ms M and her partner (neither of which I will cover in any further detail given the other complaint Ms M has made).

In March 2023, Ms M decided to formally complain to MF after reviewing the online valuation of her investment ISA. In summary, she said that she was surprised her investment had gone down by so much and, having looked at the funds her savings were invested in, stated that she believed MF had invested her savings outside of the level of risk that she was prepared to take.

After reviewing Ms M's complaint, MF concluded that they were satisfied they'd done nothing wrong. They also said, in summary, that their adviser had completed a risk questionnaire with Ms M and the funds that they had recommended matched overall, the same 'high medium' risk level as her stated profile. Given that Ms M had sufficient emergency monies remaining after their recommendation, MF said that they felt their advice was appropriate.

Ms M was unhappy with MF's response, so she referred her complaint to this service. In summary, she explained that she didn't believe MF's original advice was appropriate because the level of risk they'd concluded she was happy to invest at was above what she was actually content with.

The complaint was then considered by one of our Investigators. In summary, he concluded that MF hadn't treated Ms M fairly because as an inexperienced, first-time investor, it appeared that MF had committed too much of her savings to risk based investments, which on the face it, contained high levels of equity content. He also explained that he didn't feel the level of risk that MF had categorised Ms M as, was appropriate.

MF, however, disagreed with our Investigator's findings. In summary, they said they'd established Ms M's risk profile through the use of an electronic risk profiling tool and as such, were satisfied it was accurate. In addition, they said the funds that Ms M invested in mirrored her chosen risk profile and also went on to say that they felt Ms M's complaint was about the performance of her funds which was as a consequence of the markets in general rather than their original advice.

Our Investigator was not persuaded to change his view as he didn't believe that MF had presented any new arguments that he'd not already considered or responded to. MF then asked the Investigator to pass the case to an Ombudsman to review that outcome.

## What I've decided – and why

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

I have summarised this complaint in less detail than Ms M has done and I've done so using my own words. The purpose of my decision isn't to address every single point raised by all of the parties involved. If there's something I've not mentioned, it isn't because I've ignored it - I haven't. I'm satisfied that I don't need to comment on every individual argument to be able to reach what I think is the right outcome. No discourtesy is intended by this; our rules allow me to do this and it simply reflects the informal nature of our service as a free alternative to the courts. Instead, I will focus on what I find to be the key issue here, which is whether the advice provided by MF was suitable for Mrs M, particularly when considering her attitude to risk and wider circumstances.

My role is to consider the evidence presented by Ms M and MF in order to reach what I think is an independent, fair and reasonable decision based on the facts of the case. In deciding what's fair and reasonable, I must consider the relevant law, regulation and best industry practice, but it is for me to decide, based on the available information that I've been given, what's more likely than not to have happened. And, having done so, I'm upholding Ms M's complaint and it's largely for the same reasons as our Investigator. I'll explain why below.

I think that MF failed to take reasonable steps to ensure that their recommendation was suitable for its client. From what I've seen, I don't believe that MF met the Financial Conduct Authority's Conduct of Business 9.2.1 rule, which explains that firms must ensure the recommendation is suitable for the client's knowledge, experience, financial situation and their investment objectives.

I've looked closely at Ms M's circumstances at the time of the advice in June 2021. At that point, she was 26 years old, held £40,707 in cash (£34,207 of which was in a cash ISA and she owned 50% of £13,000 in a joint deposit account with her partner), she had an outstanding mortgage of £158,366 and aside from her employee pension scheme, she'd not invested previously and was therefore considered to be an inexperience investor. MF's adviser noted that she earned a salary of £40,000 per annum and had a household monthly net disposable income (of £1,450 and no major expenditure planned in the foreseeable future. The fact-find noted that she was in good health and happy to invest for the medium to long term.

MF’s suitability letter explained that Ms M’s primary aim was to achieve better returns beyond what she was receiving within her cash ISA. So, based on Ms M’s circumstances at the time, it seems to me that she did have the capacity and desire to explore investing some of her monies to achieve her goal.

During their discussions, MF completed a questionnaire with Ms M to establish how much risk she was prepared to take with her investment. Their assessment determined that she had an attitude to risk of six, or ‘high medium’. Having reviewed the questionnaire MF completed with Ms M, I think there’s some inconsistencies in the responses she provided compared to the end output:. Of the ten questions Ms M answered, two were at odds for a consumer willing to take risk with their monies:

*“I would rather know that I was getting a guaranteed rate of return than be uncertain about my investments – Agree”.*

*“I do not feel comfortable with financial uncertainty - Agree”.*

I don’t think these statements are consistent with a consumer happy to take the level of risk MF’s recommended portfolio of equity based investments represented. MF have explained that they’re satisfied with the accuracy of Ms M’s risk profile because their electronic questionnaire calculated the ‘high medium’ score off the back of her answers to the questions. But, the FCA has previously cautioned firms about relying solely on the output of electronic risk scoring questionnaires and whilst they’ve acknowledged their importance in the advice process, they should only be considered as the starting point for establishing the consumer’s final attitude to risk. I think Ms M’s responses to those two questions should’ve put MF on a path of discovery that the ‘high medium’ output was too high.

At the very least, I would have expected the inconsistencies outlined above to prompt MF to discuss the output with Ms M in detail, in order to fully ascertain the level of risk she was willing and able to take and then document that thoroughly within the suitability report. Whilst MF say that they discussed Ms M’s risk profile in detail, I think on balance, it is more likely than not that she wasn’t sufficiently interrogated on those inconsistencies because the file is silent on the output of any conversation. Given Ms M had never invested previously (beyond her autoenrollment pension) and held all her savings in cash, I think the jump from no risk to ‘high medium’ for these funds was a leap too far for her bearing in mind her lack of experience.

Following MF’s advice, Ms M found herself with 84% of her accessible wealth in risk-based investments. And, whilst the consumer had a healthy disposable income (£1,450), which on the face of it would’ve lessened the impact of the high asset concentration as time passed, I’m mindful of the fact that nearly a third of that disposable income was earmarked to fund the new pension contributions that MF had also recommended at the time. So in my view, it wasn’t appropriate for a first time, inexperienced investor to commit such a high proportion of their overall wealth to equity, risk-based investments.

I also think that’s borne out in Ms M’s response to the additional question in MF’s risk tool:

*“I would be happy investing a large proportion of my income / capital in a high-risk investment – Disagree”.*

In addition, when assessing Ms M’s capacity for loss, when asked about the goals for her monies, she selected the response: “*Any losses from this investment would reduce my* *standard of living*". Also, when asked: "*How much of your investments could you afford to lose without reducing your future standard of living*", Ms M answered, "*I could afford a small loss*".

And, whilst the portfolio that MF ultimately recommended wasn't necessarily 'high risk' by the nature of the funds it invested in, they did commit a 'large proportion' (84%) to risk-based assets that were subject to market fluctuations. And, when economic events dampened the value of Ms M's portfolio, she complained explaining that MF had exposed her savings to an unnecessarily high level of risk which, she says wasn't clear to her at the time of the advice. And, I can see why.

MF recommended that Ms M invest into four funds within the investment ISA in differing proportions – Baillie Gifford Managed B Acc (35% of her funds), Liontrust Sustainable Future Managed (32%), Sarasin Global Equity Real Return (16%) and Vanguard LifeStrategy 80% (15%). Whilst the equity content of each of the four funds will change over time, the Baillie Gifford and Liontrust funds work on the basis that up to 85% of the monies can be invested in equities at any one time, the Sarasin fund typically invests at least 75% in equities and the Vanguard fund 80% in equities.

And, whilst I appreciate the equity content that I've noted is the maximum the funds hold and from time to time they could hold less, from what I've seen, all four of the funds appear to hold equities at the higher end of their permitted thresholds and as such, are likely to be more susceptible to market movements. And that's why Ms M has seen her monies vary in value over the last 18 months, particularly in light of recent economic conditions. Overall, the portfolio was likely to leave over 80% of Ms M's money exposed to stock market movements and the majority of the overall investment was in funds that invested in individual shares, including a healthy amount of overseas and emerging market exposure. In addition, over a third of the investment, in the BG fund, was in an "aggressive" fund targeting "growth" stocks. While the potential rewards were reasonable, as with everything, that reward comes at the cost of greater risk to the consumer's capital. As it is reasonable to conclude that Ms M was more likely to have been more comfortable with a more cautious approach, it therefore follows that I don't think the funds that MF recommended were appropriate given the high levels of equity content that they contained.

<u>Summary</u>

I'm of the view that the recommendation made by MF exposed Ms M to a greater level of risk than she was willing or able to take – she was an inexperienced investor but following their interactions, she found herself in a position where the majority of her savings had been committed to risk-based investments, and those investments were skewed heavily to equity content funds. Overall, this portfolio meant that she was risking making more than the "small loss" she said she could afford, and wasn't compatible with someone uncomfortable with uncertainty.

I'm therefore of the view that MF should take the following steps to put things right for Ms M:

**Putting things right**

**Fair compensation**

In assessing what would be fair compensation, I consider that my aim should be to put Ms M as close to the position she would probably now be in if she had not been given unsuitable advice.

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

**What must MF do?**

To compensate Ms M fairly, MF must:

- Compare the performance of Ms M's investment with that of the benchmark shown below and pay the difference between the *fair value* and the *actual value* of the investments. If the *actual value* is greater than the *fair value*, no compensation is payable.

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

- Pay to Ms M £150 for the distress and upset that seeing her savings fall in value.

Income tax may be payable on any interest awarded.

| Portfolio name | Status | Benchmark | From ("start date") | To ("end date") | Additional interest |
|---|---|---|---|---|---|
| AJ Bell ISA | Still exists and liquid | For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds | Date of investment | Date of my final decision | 8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance) |

***Actual value***

This means the actual amount payable 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, MF should use the monthly average rate for one-year fixed-rate bonds as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

Any additional sum paid into the investment should be added to the *fair value* calculation from the point in time when it was actually paid in.

Any withdrawal from the MF should be deducted from the fair value calculation at the point it was actually paid so it ceases to accrue any return in the calculation from that point on. If there is a large number of regular payments, to keep calculations simpler, I'll accept if MF totals all those payments and deducts that figure at the end to determine the fair value instead of deducting periodically.

**Why is this remedy suitable?**

I have decided on this method of compensation because:

- Ms M wanted Capital growth with a small risk to her 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 her capital.

- The FTSE UK Private Investors Income ***Total Return*** index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds. It would be a fair measure for someone who was prepared to take some risk to get a higher return.

- I consider that Ms M's risk profile was in between, in the sense that she was prepared to take a small level of risk to attain her investment objectives. So, the 50/50 combination would reasonably put Ms M into that position. It does not mean that Ms M would have invested 50% of her 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 Ms M could have obtained from investments suited to her objective and risk attitude.

**My final decision**

I uphold Ms M's complaint. My decision is that Morton Hill Limited, trading as McKnight Financial, should pay the amount calculated as set out above.

Morton Hill Limited, trading as McKnight Financial, should provide details of its calculation to Ms M in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms M to accept or reject my decision before 10 March 2024.

Simon Fox
**Ombudsman**