

The complaint

Mr L1 complains that Hargreaves Lansdown Asset Management Limited (HL) gave misleading information about an investment he bought for his children, Mr L and Miss L. He says they'd now made a substantial financial loss as a result of this misleading information and would like compensation.

What happened

The investment Mr L and Miss L bought from HL was called the Woodford Equity Income Fund (WEIF) and was managed by Neil Woodford, who left Invesco Perpetual in 2013 to set up Woodford Investment Management ("WIM"). The WEIF was launched in May 2014, with a £1 per unit fixed offer price until 18 June 2014. The Authorised Corporate Director (ACD) of the fund was Capita Financial Managers, later known as Link Fund Solutions.

The WEIF broadly tracked the benchmarks (albeit whilst providing a greater return and experiencing some more volatility) until the second half of 2017, when there was a significant fall which was not experienced by the benchmarks. It began to significantly underperform benchmarks from early 2018 and the performance followed a very different pattern to the benchmarks from early 2019 to the date of suspension.

Alongside this, the fund began to see significant outflows from mid-2017, falling from around £10bn of assets under management to around £3bn in two years.

In June 2019 the extent of those outflows - and the portion of the WEIF's assets which were not liquid - led Link to decide to suspend trading in the fund. Link removed WIM as the investment manager around this time.

The fund did not trade again. Later in 2019, Link decided to liquidate the fund. Investors have since received payments as and when the fund's assets have been sold. A small amount remains invested in assets which are not liquid i.e. cannot currently be sold. A scheme of arrangement between investors and Link has now been sanctioned by the court and will conclude the wind up of the fund with further distributions being made to investors who held units in the fund at suspension.

HL's communications relating to the WEIF

HL's relationship with WIM and the WEIF began prior to the fund's launch. HL met with WIM in early 2014 and decided to promote the WEIF to its customers and visitors to its website ahead of the fund's launch.

The WEIF was the subject of, or featured in, many communications from HL over the period from the fund's launch to its suspension. HL's communications relating to the WEIF can be categorised broadly as follows:

- Promotion of the WEIF at its launch by letter and through website articles and emails.

- Ongoing promotion of the WEIF through website articles (and, in some instances, emails alerting the recipient to the article).
- Updates on the WEIF through website articles (and emails alerting the recipient to the article).
- The inclusion of the WEIF in “best buy” lists – called the Wealth 150 (which had a subset of discounted funds called the Wealth 150+) and, later, the Wealth 50 – both of which were shared on its website, through emails and via Wealth Reports, which were included in the Investment Times sent to its clients by post.

The Wealth List

HL published a list of what it considered, in its view, to be the “best” or “favourite” funds. This was initially called the Wealth 150 (and a subset of this, featuring discounted management charges for HL clients, the Wealth 150+) then later the Wealth 50 – I’ll refer to these generally as the Wealth List. The WEIF featured on the Wealth List from its launch until its suspension.

I understand the list was available on HL’s website to any visitor and also sent to all customers on its general mailing list who had elected to receive communications, alongside the bi-annual Wealth Reports published by HL. HL says the list was updated from time-to-time with funds being added or removed as a result of the ongoing cycle of review, monitoring and analysis of funds by its investment team.

As part of its ongoing research HL met with WIM to discuss the WEIF on a number of occasions.

Mr L and Miss L’s dealings in the WEIF

In October 2016 Mr L1 bought around £690 worth of units in the WEIF in Mr L’s Junior Stocks & Shares ISA (JISA). In the same month, Mr L1 also bought £1,313 worth of units in the WEIF in Miss L’s JISA.

Mr L’s and Miss L’s complaint to HL and its response

In 2019, shortly after the suspension of the WEIF, Mr L1 made a complaint to HL about its promotion of the WEIF and its communications around it, in particular its Wealth Lists.

HL looked into Mr L1’s complaint but didn’t think it had done anything wrong. In short it said that the Wealth Lists were “*tools for clients to use in making decisions when choosing from the full range of funds available on our platform*”. It acknowledged the WEIF had experienced a “*difficult period of performance*” but emphasised that although it had a reasonably held conviction in the prospects of the WEIF outperforming its benchmark, it provided an “*execution-only service*”, which meant that it was not providing investment advice or making personal recommendations.

It said that the information it provided about the WEIF on its Wealth Lists or in other communications was not designed to be taken as a personal recommendation to deal in a fund, and was provided to them in order to help them decide whether or not to invest.

Mr L1 remained unhappy and the complaint was referred to this service.

One of our investigators looked into the complaint but didn't consider it should be upheld. In short, he concluded that HL's communications met its regulatory obligations and were clear, fair and not misleading.

Mr L1 didn't agree and asked for an ombudsman's decision. In summary he said:

- He continued to keep his children's JSAs invested in the fund because it was still on HL's recommend funds list – if it had been removed, he would also have sold his children's holdings.
- The initial investment was driven by the WEIF's inclusion on HL's top 50 funds. So it was clear that HL's communications influenced the decision to invest in the WEIF.
- HL ought have been more thoughtful in its recommendations, and the investigator was wrong to suggest that its top 50 list didn't influence investors. He said that for HL to have included the fund on the list even after it was "*breaching certain parameters*" was questionable and misleading.
- There would've been thousands of investors who would've been influenced by HL's investment recommendations, and who "*trusted HL to include well run funds on the list*". HL ought to have at least removed the WEIF from its list "*when the balance of the portfolio became poor*" – and then informed investors.

As agreement couldn't be reached, the case was passed to me to decide.

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 understand Mr L1's strength of feeling on the complaint and why he considers HL is responsible for the losses Mr L and Miss L have experienced on the WEIF. However, for the reasons I set out below, I'm not persuaded Mr L1 was misled into investing (or remaining invested) in the WEIF – and consequently, I'm satisfied the losses arose due to the poor performance of the investment and its underlying holdings, which HL had no responsibility for.

I've first set out what I consider the relevant regulatory obligations that HL's communications needed to meet.

What are the relevant regulatory obligations?

I think the following regulatory requirements are of particular relevance to my assessment of whether HL acted fairly and reasonably in its dealings in this case.

The Principles for Businesses, which are set out in the FCA's handbook "are a general statement of the fundamental obligations of firms under the regulatory system" (PRIN 1.1.2G). I consider that Principles 6 and 7 are of particular relevance to this complaint. They say:

- Principle 6 – Customers' interests – A firm must pay due regard to the interests of its customers and treat them fairly.
- Principle 7 - Communications with clients – A firm must pay due regard to

the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

I have also taken into account the FCA rules for firms carrying on investment related business set out in the Conduct of Business Sourcebook (COBS). In particular, COBS 4.2.1R, which sets out the requirements on authorised firms, like HL, when communicating with clients. COBS 4.2.1R(1) says:

“A firm must ensure that a communication or a financial promotion is fair, clear and not misleading.”

COBS 2.1.1R (1) (the client's best interests rule) is also relevant to this complaint. It says:

“A firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule).”

My findings

I should say firstly that the investigator didn't conclude that HL's Wealth Lists, or its commentary about the WEIF, didn't influence Mr L1's investment decisions on his children's behalf. I accept that the investments were made by taking into account what HL said about the WEIF, including what it said about its long-term prospects.

But the rules (set out above) that HL was required to adhere to when making these communications required HL to issue communications which were clear, fair and not misleading. This means that as long HL's communications during the relevant period were factual and gave a balanced view of its assessment of the WEIF, then it didn't do anything wrong.

It's clear that HL provided significant positive commentary about Woodford and the WEIF prior to Mr L's and Miss L's investment in 2016, and it obviously believed that Woodford's track record, as well as the objective and performance of the WEIF between 2014 and 2016 were such that it continued to be a fund that it thought met its criteria for inclusion on its Wealth Lists.

The evidence I've seen shows that whilst HL met numerous times between 2014 and 2016 with Woodford and had frank conversations about his management of the fund, its views were largely consistent with what it was telling its customers.

In December 2016, shortly after Mr L and Miss L invested in the WEIF, HL said on its website that the WEIF was “*not a typical equity income fund*” and said that unlike most equity income funds which were exposed to large high-yielding companies, “*only around 50%*” of the WEIF was invested in this area. The remainder was “*invested in small and medium sized companies, or those not listed on the stock market*”.

So I think it's fair to say that Mr L1, who was monitoring Mr L and Miss L's investments, ought to have known that the WEIF had certain risks associated with its investment strategy.

HL was explicit that the fund had a “*significant bias to smaller companies relative to the FTSE All Share Index which adds risk, and also has more invested in medium sized companies than the index*”. Ultimately HL's view was that this approach would “*add significant value for investors able to withstand the additional risk and volatility that comes from investing in smaller and unquoted companies.*”

Having reviewed the evidence of HL's meetings with WIM in 2016, I can see that in summary it was aware that the WEIF was no longer a typical equity income fund. I can also see that it knew there had been a shift towards small cap and growth stocks which it had not expected – and it recognised that in the event of significant outflows, that proportion would increase and potentially affect WIM's ability to invest further. HL was also aware that its customers might not know how the fund had changed – and it agreed to take steps to address this. It's clear to me that the update above was designed to draw these concerns to their customer's attention.

But HL also continued to hold the view that the WEIF was still an investment that would add value for investors – and I'm satisfied it held that view internally and so it was clear, fair and not misleading to have continued to say that in its updates. It was obviously for Mr L1 to decide for himself whether the risks and the features of the WEIF which HL was describing to him were right for his children's investments and their circumstances.

I acknowledge that in 2017 the WEIF began to underperform its benchmark, but I'm satisfied that HL's continuing communications about the fund remained balanced. It was clear that it viewed the WEIF as a long term investment and explained in its June 2017 update that Woodford had *“a long history of making big stock or sector bets, and while these decisions have at times taken time to come to fruition, they have added significant value for investors over the long term”*.

In an article it published in September 2017 on its website, it explained that *“judging a fund manager over a time period of a few months is folly, especially one with such a long and distinguished track record”*. This article explained that Woodford had experienced poor performance in the past, and that it was *“quite right to question any fund manager on their performance”* which HL said it had done. But it explained that his approach involved seeking out undervalued companies and this strategy had *“seen his investors well-rewarded over the long term”*.

In its November 2017 Wealth Report HL said that performance *“over the past year has been disappointing relative to the FTSE All Share Index”* and that some of Woodford's stock selections had under-performed. But HL continued to have *“faith in his abilities to deliver for investors”*. In my view HL was entitled to continue to believe in the long term prospects of the WEIF – and I'm not persuaded it was misleading for it to communicate its view that, over the long term, the WEIF would still be a good investment. I'm not persuaded that this belief, and its communication of it, was inconsistent with the obligations I've set out above.

I acknowledge Mr L1 has raised the issue of Woodford breaching *“certain parameters”* and the balance of the fund becoming *“poor”*. But it's important to highlight that HL wasn't managing the WEIF, and had no say over what stocks Woodford was choosing to buy.

In December 2017 it said on its website that the WEIF wasn't *“a typical equity income fund”* and highlighted that around 9.5% of the fund was in unquoted companies. HL explained clearly that *“small and unquoted businesses are typically considered higher-risk because their shares are difficult to sell”*. And it concluded that Woodford's approach would *“result in periods of poor performance”* but it was *“premature to write Neil Woodford off”*.

The key issue here is that none of these updates differed markedly from the concerns HL was expressing to Woodford throughout the year and from its internally held view that whilst the fund was suffering from a period of poor performance, HL remained of the view that over the long term the investment would come good. The evidence shows that HL was aware of the WEIF nearing the 10% limit and was clearly aware of the poor performance of the fund.

I've seen evidence that it robustly challenged WIM when necessary, but it was also reassured by WIM's responses to those concerns – in particular in relation to the levels of unquoted stock. Ultimately, HL continued to believe that periods of poor performance were temporary, and that whilst it was important to ensure it was open about the nature of the WEIF and how it had changed, it continued to believe it was a good investment for the long term.

It's clear to me that Mr L1 had sufficient information from these updates to know that the WEIF was not a typical equity investment – and that there were specific risks in the way the WEIF was managed that he needed to be comfortable with.

In that context, I don't agree the message that HL continued to believe the fund would improve its performance of the long term was misleading, because HL believed that to be the case – and was entitled to that reasonably held belief.

And I'm satisfied that HL's communications in 2018 and 2019 were equally clear, fair and not misleading. In March 2018, for example, HL published an update following WEIF's change of sector. It clearly explained how almost *"40% of the fund is invested in small and mid-sized lower-yielding companies"* with *"an additional 10% invested in companies not yet listed on the stock market"*. And the same update was clear that HL accepted Woodford's approach would *"lead to tough periods of performance"* but that it remained *"comfortable with the inclusion of unquoted companies"* although it did not *"want to see them increase as a proportion of the fund from here"*. It reminded investors to *"ensure they are comfortable with the investment approach and risks"*.

The evidence I've seen of HL's internal views and the meetings it had with WIM during 2018 show that HL was largely reassured that WIM had taken onboard its feedback, particularly in relation to continued investment in unquoted stock. And this is clearly reflected in the communication above. Internally it continued to believe that the fund would come good in the long term, but it acknowledged that it needed to ensure clients were aware of the nature of the fund, the need to diversify and the strategy WIM was following. In my view, the updates I've quoted above achieve this in a clear, fair and not misleading way.

In 2019 HL issued an update in January in which it explained its recent catch-up with Woodford. It said that although it had been a long-term supporter of Woodford, *"his funds have recently performed poorly"* and so it had been *"an uncomfortable time to hold the fund and our own conviction has been tested"*. The update then went on to explain why it continued to keep the fund on its Wealth 50 and provided a detailed explanation of how the WEIF had changed since its launch, and some of the inherent risks of Woodford's approach to investing. And it said it was clear that some of Woodford's investments hadn't *"paid off"* and importantly highlighted to investors *"the importance of having a diversified portfolio, spreading your investments amongst managers that invest differently"*.

It concluded by saying that it was *"understandable that some investors are getting impatient with Woodford"* and that it had also *"been disappointed with recent performance"*. But it said that its approach was to back proven managers for the long-term and *"as part of a diversified portfolio, we still think Woodford has a place"*.

Crucially, it said:

"We could be wrong. If we are we'll put our hands up. It might be tempting to change our opinion now to be rid of the current discomfort, but we don't think it would be the right thing to do".

Further updates in March highlighted that Woodford was experiencing “*his worst spell of performance*” and the fact that HL had been urging Woodford to “*address the weighting [of unquoted] stocks in his portfolio*” – and overall it said that Woodford had “*shown an ability to make the big calls right, and when he does, investors profit*”.

During this period, the evidence shows that HL was in regular contact with Woodford in a bid to understand the challenges he was facing in managing the fund and to ensure that its faith in his ability to turn things around wasn’t mis-placed. The suspension of three stocks on the Guernsey exchange was a significant cause for concern – but this suspension was only temporary. Furthermore, although it discussed whether the time had now come to remove the WEIF from its Wealth List, it’s clear that internally it also considered the likelihood that the WEIF would recover. It had been reassured by WIM that it would deal with the level of unquoted stock in the portfolio – and HL told its clients this. I’m satisfied at this point, HL was clearly finding a way to balance communicating the risks and its concerns to consumers, while at the same time being open that it continued to believe that the WEIF would recover in the longer term.

When looking at the updates it provided, I think it’s clear from HL’s updates that there were risks in remaining invested in the WEIF, and the performance had now been disappointing for some time. But it was entitled to tell its clients that it believed the fund would recover – because that is what it believed internally at the time, for reasons which it gave in its updates.

Overall it’s clear that there were periods between 2016 and 2019 when HL raised concerns with Woodford, for example around the level of unquoted stock in the WEIF, but it explained these concerns in its public updates or Wealth Lists – at the same time, it held the view that whilst there were some concerns in the short term, over the long term the WEIF would end up being a good investment for its clients. HL was entitled to hold that view, and I’ve seen insufficient evidence that it came to that conclusion unreasonably, capriciously or in a way that was not genuinely based on its assessment of the WEIF and its future prospects.

Whilst I appreciate HL’s view has turned out to be wrong, largely as a result of the liquidation of the fund which was not something it had anticipated, I don’t consider that means its communications were not clear, fair and not misleading.

In my view it clearly explained the risks of the fund, the areas where it had concerns and the reasons why it thought it was still worthwhile to hold it as part of a diversified portfolio.

It was then for individual investors to decide, for themselves, whether in light of that information, the risks as described as well as the ongoing period of under-performance, holding the WEIF remained suitable for them.

I appreciate my conclusions will be disappointing to Mr L1 and I understand why he feels HL ought to be responsible for the losses to his children’s investments. But I’m satisfied that the financial loss Mr L and Miss L have experienced was not caused by something HL did or didn’t do or because it misled Mr L1 in anyway. I’m satisfied those losses were caused by the performance of the underlying investments in the WEIF, and its subsequent liquidation by the authorised corporate director.

My final decision

For the reasons I’ve given, I don’t uphold Mr L and Miss L’s complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr L and Miss L to accept or reject my decision before 4 June 2024.

Alessandro Pulzone
Ombudsman