

The complaint

Mr and Mrs M have complained about the advice they received in 2016 and 2017 from Hargreaves Lansdown Advisory Services Limited ('HL') to invest in the Woodford Equity Income Fund ('WEIF').

What happened

Mr and Mrs M first met with an HL adviser in late 2015 to discuss ways in which to use their assets to produce an income after Mr M had stopped working. They were seeking to achieve an income of £90,000 per year in retirement. Of this amount, around £25,000 per year was calculated to be coming from defined benefit pension schemes.

In February 2016 the adviser recommended that Mr M transfer funds held under a defined contribution plan and a personal pension plan into his existing HL Vantage self-invested personal pension ('SIPP'). Tax free cash was to be taken and the residual pension fund was to be invested in an HL drawdown account. The tax free cash itself was to be invested across HL stocks and shares ISAs that Mr and Mrs M each held, and into Mrs M's HL fund and share account.

The adviser recommended that the drawdown account, the ISAs and the fund and share account be invested in a portfolio of funds with an objective to achieve income and growth. The funds were selected by HL's investment research team. Within the drawdown account, HL proposed 13% of the fund of £447,962 (valued at the time of the report) should be invested in the WEIF. For the ISAs and the fund and share account, 15% of the total funds of £342,112 was to be invested in the WEIF.

In May 2016 following a further meeting, the HL adviser recommended that Mr and Mrs M place £600,000 into a Canada Life bond in joint names. The funds came from a portfolio of cash and investments that Mr and Mrs M held elsewhere. The bond was to provide an income of £30,000 each year. HL recommended a portfolio of funds to invest the bond into, proposing that 13% be invested in the WEIF.

Mr and Mrs M initially signed up to HL's regular review service to receive an annual review of their financial circumstances. As part of this service they met the adviser in February 2017. The adviser recommended that Mr and Mrs M each invest £15,240 into their ISAs prior to the end of the tax year. HL recommended a portfolio of income and growth funds. This included investing 13.5% of the new ISA funds into the WEIF.

After receiving this periodic suitability review in February 2017 from HL, Mr and Mrs M decided not to continue to receive regular reviews.

By way of background in terms of the WEIF, this fund was managed by Neil Woodford. It was launched in May 2014. 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 to trading in the fund to be suspended. There was also a change of investment manager around this time.

The fund did not trade again, and later in 2019 it was decided that it should be liquidated. 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 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.

In 2020 Mr and Mrs M complained to HL that the advice they had been given to invest in the WEIF was unsuitable for their aim to obtain an income in retirement. They said the WEIF had a high risk profile but they'd not been made aware of this. Mr and Mrs M also complained that HL had continued to promote the fund in its published Wealth Lists.

I should explain that Mr and Mrs M's concerns that HL continued to promote the WEIF within its Wealth Lists has been considered by this service in a separate complaint against a different part of HL. That aspect of their original complaint does not therefore form part of the subject matter of the complaint I am considering here. Under this complaint, I have considered Mr and Mrs M's concerns about the initial recommendations they received from HL to invest in the WEIF in 2016 and 2017.

In response to those concerns, HL stated that it considered the recommendations to invest in the WEIF as part of a strategy to provide an income in retirement were suitable, and in line with Mr and Mrs M's attitude to risk. It said that its investment team had included the WEIF in the portfolio recommendations it had made on the basis of "*Neil Woodford's proven track record as a talented stock picker.*" HL said it believed that the WEIF had the potential to outperform its benchmark.

HL commented that once Mr and Mrs M had contacted it in February 2017 and asked to be removed from its review service, the service they received was 'execution only', meaning that HL no longer provided ongoing personalised investment advice. It said that it had always made it clear there were risks with investing in the WEIF and there were no guarantees about its performance. Under the execution only service, HL said the decision to remain in the fund rested with Mr and Mrs M.

Unhappy with HL's response, Mr and Mrs M brought a complaint to this service.

In his initial consideration of this case, our investigator commented to Mr and Mrs M that when a business recommends funds to clients, it's inevitable that some will not perform as well as hoped, but this doesn't necessarily mean that it was wrong to recommend a fund. He also stated that higher risk investments can form part of a medium or low risk portfolio, and that he would be assessing the suitability of the overall portfolio recommended by HL.

Mr M responded that HL provided advice at fund level, based on what it said about its investment team's expertise, and that consequently it wasn't appropriate to only look at HL's recommendation at portfolio level. He also said that at the dates that HL gave advice to invest in the WEIF, the fund had already had a "*dramatic Style shift towards much higher risk and speculative shares with no or low liquidity.*" Mr M said that this led to HL providing

inappropriate advice. He highlighted that HL had advised him and his wife to invest almost £200,000 into the WEIF across the products it had made recommendations for.

Mr M said that he had expected each fund recommended to provide a consistent and reliable retirement income. He stated that at launch the WEIF *“was invested heavily in safe, large cap shares but this changed quickly and HL didn’t appreciate the implications of these changes”*. Mr M forwarded an article from an online research platform that he said showed the WEIF had drifted from an initial focus on large cap stocks to speculative and unquoted stock. He also commented that there was a difference between a fund not performing well compared to the performance that the WEIF experienced.

Mr M said the key issue was that the liquidity of the WEIF meant it couldn’t cope with withdrawal requests. He commented that HL had clear evidence of a lack of liquidity in the fund when it recommended investing in it to him and Mrs M.

Our investigator did not uphold this complaint. He reiterated that he considered it was appropriate to consider whether the overall portfolios recommended by HL were suitable. In terms of the asset mixes recommended by HL for the various portfolios, and taking into account Mr and Mrs M’s attitude to risk and capacity for loss, the investigator stated that the overall portfolio recommendations were suitable. He said that Mr and Mrs M’s objective to reinvest their existing funds to draw an income and grow capital was always likely to involve an element of risk.

In terms of HL’s recommendation to invest in the WEIF, the investigator’s view was that placing between 13-15% of each portfolio into a single fund did not materially increase the risk level implied by the asset mixes which had been agreed. He said there was still sufficient diversification. The investigator stated that HL had identified the WEIF as having the potential to perform well over the long term. Although the investigator described the fund as being higher risk, holding equities only and with around half being in smaller or medium sized companies, he didn’t consider this made the fund unsuitable for Mr and Mrs M, in the context of their overall portfolios. He said the fund fact sheet HL had provided had explained the composition of the WEIF, including its holding of unlisted companies.

Mr and Mrs M disagreed with the investigator’s findings. Mr M said that if the WEIF had retained its original investment strategy it would have been suitable, but by the time HL advised investing in it, its strategy had dramatically changed. He said that HL knew this but did not tell him and Mrs M. Mr M commented that the fact the WEIF had ceased to be classified as an income fund demonstrated it had significantly changed its investment strategy. He questioned what HL knew about the WEIF’s strategy when it provided the advice that it did.

Referring to the online research source he had previously mentioned, Mr M said that in 2014 the WEIF had had under 20% invested in unquoted and speculative stocks, but by 2017 this had grown to over 40%. He said HL had clear evidence of this when it recommended the fund. Mr M commented that Woodford’s track record was established through investing *“in low risk, dividend paying companies. It wasn’t made in higher risk investments.”* He said to base a recommendation upon a track record was an error.

Mr M quoted from HL documents provided to him in December 2015 stating that the WEIF invested in some of the UK’s largest and most profitable companies, providing generous yields, but also looked for *“tomorrow’s dividend winners amongst higher-risk smaller and medium sized companies.”* He said that this didn’t imply that by 2017 over 40% of the fund *“would be invested in unquoted and highly speculative illiquid investments.”* Mr M also questioned the relevance of his and Mrs M’s capacity for loss when deciding whether the recommendation to invest in the WEIF was appropriate.

The complaint was passed for review by an ombudsman.

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 acknowledge what Mr M has said about the overall advice from HL to invest in the various portfolios not being key to this complaint. He has said that the crux of this matter relates to the suitability of HL recommending investment in the specific fund that he and Mrs M have complained about, that being the WEIF. Whilst I understand his reasons for saying this, my view is that in assessing this complaint, it is necessary for me to consider the full recommendations made by HL in 2016 and 2017. I do not consider that it is reasonable to look at the advice to invest in the WEIF in isolation, because the financial need that HL was attempting to address was to secure a sufficient income for Mr and Mrs M from all of the financial assets available to them. I do need to consider whether investing in the WEIF was a suitable recommendation from HL, but within that wider context.

HL's adviser's report in February 2016 confirmed that Mr and Mrs M were seeking to generate an income of £90,000 net of tax from their assets, giving Mr M the option not to return to work. Around £25,000 per year of this income would come from defined benefit pension schemes. HL recommended transferring two of Mr M's other existing pension plans into his HL SIPP. Tax free cash from these funds was to be taken and invested in Mr and Mrs M's ISAs, and Mrs M's fund and share account. The residual pension funds were to be placed in a drawdown account.

These new investments were to be placed in portfolios seeking income and growth. In total the net income from these investments was estimated to be around £28,500 per year. At this time Mr and Mrs M held money outside HL that they were intending to invest in an offshore bond to provide a further income of £30,000 per year. The combined income from their HL accounts, the defined benefit pensions and the proposed offshore bond totalled over £80,000 a year. The adviser proposed that Mr and Mrs M's surplus cash (recorded as being £170,000) could be used to top up income if necessary.

The adviser discussed with Mr and Mrs M their attitude to investment risk. It was noted that Mr M's previous employment meant he was a knowledgeable and experienced investor, with Mrs M being less knowledgeable than her husband. It was also noted that because the income from Mr M's defined benefit pensions covered essential expenditure, Mr and Mrs M had the capacity to deal with potential losses. HL recorded that Mr and Mrs M were comfortable accepting volatility because they were investing for income throughout retirement and understood they would experience this.

HL recommended that the portfolios it was proposing should have an asset mix of 15-25% in fixed interest and 75-85% in managed equities. Later in 2016 when HL recommended investment in the Canada Life bond, it proposed a portfolio of 15% fixed interest, 79% managed equities and 6% cash (to pay the first year of income plus charges). For the ISA investments recommended by HL in February 2017, 29% was to be in fixed interest, 70% in managed equities and 1% in cash.

Taking into account Mr and Mrs M's objectives to generate income from their funds and their attitude to and tolerance of investment risk, my view is that HL's recommendations in 2016 and 2017 were suitable for their identified needs. Based on the information the adviser had recorded about Mr and Mrs M's financial position and their aims, in my view the emphasis on investment in managed equities was reasonable. Mr and Mrs M also had significant cash

reserves that they could draw on in the event that their portfolios did not provide the required income levels that they were seeking.

I note that Mr and Mrs M are not disputing the overall recommendations they received from HL in 2016 and 2017. However, it is the inclusion of the WEIF within the recommendations that they are unhappy about, because they say the risk of that fund was too high and that it was inconsistent with their need for a retirement income. They also say that HL knew the WEIF had undergone an investment strategy shift to higher risk assets by the time its recommendations were made to them.

The proportion of the portfolios that were invested into the WEIF ranged from 13-15%. I would agree with the investigator that, when looking at the range of other funds also recommended by HL at the same time, the portfolios had sufficient diversity, and were in keeping with the asset mixes agreed with Mr and Mrs M.

Mr and Mrs M say that the WEIF underwent a style shift between its launch and the dates when HL recommended it be included in their portfolios, making it much higher risk and reducing its liquidity. HL has commented that the Key Investor Information Document ('KIID') for the WEIF at its launch categorised it as being 6 out of 7 on the risk scale. I understand that the KIID provided to Mr and Mrs M when they invested in the WEIF showed the fund to have a risk rating of 5 out of 7. In my view both of these KIID documents made it clear that the fund came with some significant risk attached to it, based on these ratings.

In addition HL's February 2016 recommendation letter to Mr and Mrs M described the fund as containing "*many well-established businesses*", but also "*higher-risk smaller and medium-sized companies*." I appreciate that the make up of the WEIF did start to change during 2016. But a large proportion was invested in FTSE 100 stock, and even if exposure to small and medium sized companies had begun to increase, I don't consider that made it unsuitable as part of the overall portfolio that HL was recommending. And overall I consider HL did provide information that presented the WEIF as a higher risk fund.

I have thought carefully about Mr M's comments regarding the liquidity levels of the WEIF, and the impact these have had on its ability to meet withdrawal requests. He has said that HL had clear evidence of this lack of liquidity when it recommended investing in 2016 and 2017. I accept that within the portfolios, the WEIF brought some higher risk as a fund. But I also consider that the risk profile of the investments in the portfolio as a whole needs to be considered, when set against the objectives and attitude to risk of Mr and Mrs M. And overall, I don't consider HL had reason to conclude in 2016 or 2017 that the type of stock that the WEIF held meant that it should not be included as one of the funds recommended for the portfolios.

Mr M has mentioned that the WEIF ceased to be classified as an income fund. But this occurred in 2018, by which time Mr and Mrs M were no longer receiving advice from HL about their investments. Consequently there was no obligation on HL at this time to discuss whether or not this affected the ongoing suitability of holding the WEIF in the portfolios.

As Mr and Mrs M have highlighted, they invested significant sums of money across the portfolios in the WEIF. I appreciate that they will be disappointed with my findings, bearing in mind the loss they experienced from their WEIF investments. However my conclusion is that it was reasonable for HL to recommend the WEIF for Mr and Mrs M's portfolios. It considered that the fund had the potential to provide a good return, and that it was an appropriate investment to enable the portfolios to meet Mr and Mrs M's stated aims of both capital growth and income in retirement. My conclusion is that the advice provided by HL to invest in the WEIF was suitable.

My final decision

My final decision is that I do not uphold this complaint, and I make no award.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M and Mrs M to accept or reject my decision before 11 December 2024.

John Swain
Ombudsman