DRN-4679209

The complaint

Mr H complains on behalf of his daughter (Miss H) that Hargreaves Lansdown Asset Management Limited (HL) inappropriately switched her cash child trust fund (CTF) into an unsuitable investment in a junior stocks and shares ISA (JISA).

Mr H went on to say that he was 'horrified' when he subsequently discovered her monies had been invested in the Woodford Equity Income Fund (WEIF) and had significantly fallen in value – he says that's because it was done without his say so.

Mr H wants HL to reinstate his daughter's JISA to its original value.

What happened

Mr H's daughter previously held a CTF with a firm that I shall call Bank B. Her monies within that plan were invested in the stock market (although it's not clear which funds it was invested in). On 18 October 2015, Mr H signed an application to switch the CTF into a JISA. Originally, Mr H asked HL to move the existing investments directly from the CTF and into the JISA but it subsequently transpired that the CTF would need to be moved in cash.

On 31 August 2016, an order was placed online to purchase £4,000 worth of units in the WEIF within Miss H's JISA. When Mr H's daughter was approaching her 18th birthday, he contacted HL to get an update on her plan and was shocked to discover the JISA wasn't invested in cash but in the WEIF that had fallen significantly in value.

Mr H complained to HL as he was upset that her monies could have been invested in a fund which he felt they'd clearly not completed any due diligence on. However, HL didn't uphold Mr H's complaint - they explained that as an execution only customer, it was up to Mr H to make his own investment decisions. HL also provided wider information about the WEIF that Mr H's daughter's monies were invested in which they said showed that they'd shared all of the information with their consumers which they'd had available in order to help them make an informed choice.

HL also 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.

Miss H's JISA was invested in the WEIF that 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.

Unhappy with the outcome of the complaint that had been submitted to HL, Mr H raised a complaint on behalf of his daughter with this service. In summary, he said that after receiving some marketing from HL, he moved her child trust fund to the firm, but he says that he never selected an investment portfolio at the time. Mr H said that he didn't think it was reasonable that HL should've put his daughter's monies in such a fund without having done their proper research. In addition, Mr H stated that at no point did he or his daughter receive any paperwork or statements alerting them to the fact that her monies were progressively decreasing in value.

After considering Mr H's complaint, our Investigator issued an initial view on the complaint. He didn't believe from what he'd seen that Mr H's daughter had been treated unfairly. He explained that the evidence suggested that as an execution only client, HL would only invest in a fund within which they'd received instructions to do so. In addition, from what he'd seen, the information that HL had shared about WEIF had been clear, fair and not misleading.

Unhappy with that outcome, Mr H asked the Investigator to pass the complaint to an Ombudsman to consider.

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've looked closely at the nature of the relationship that Mr H had with HL. Mr H was an execution only client; that meant HL was not responsible for advising him, selecting which investments were most appropriate for his daughter or managing or providing an ongoing review of her investments. Mr H alone was responsible for deciding how much money to deposit, when to purchase investments and on what markets, monitoring those purchases, and when to make adjustments to them. So, the nature of the service that Mr H was paying for from HL meant that it was his responsibility (and not HL's) to ensure he was fully aware of the status of his daughter's investment and whether and when he needed to fund or switch investments.

Despite what Mr H has said, I think the application form that he completed when opening his daughter's JISA in October 2015 was clear that he was opening a stocks and shares ISA and not a cash ISA. In any event, it seems that Miss H's CTF was already invested in stocks and shares prior to moving to HL because her father asked HL to move the existing instruments in-specie rather than encashing what she already held. It subsequently transpired HL couldn't and the CTF had to be switched in cash to the JISA. The application form contained a declaration which required Mr H to confirm he had read HL's Terms & Conditions and Key Features of the account before committing to an investment. It also stated that HL had not provided any financial advice and Mr H signed a declaration to confirm this.

Whilst Mr H states that he never selected any investment fund for his daughter's JISA, HL have shared evidence with this service that demonstrates an internet order was placed for the WEIF on 31 August 2016. And, as Mr H was an execution only client, that meant purchases could only be undertaken by him, as the named adult on his daughter's account. As such, I'm satisfied that the reason why Miss H found herself in the WEIF was as a consequence of instructions provided by Mr H and not because of HL placing her into that fund without his approval.

In his complaint to this service, Mr H stated that at no point did he or his daughter receive any paperwork or statements alerting them to the fact that her monies were progressively decreasing in value. HL have shared a list showing the statements and literature that was posted and emailed to Mr H between May 2017 and February 2023. Aside from an investment report that Mr H says he received in November 2016, he states that he didn't receive any correspondence, either though the post or via email. I've looked closely at both the email address and postal addresses that HL used to send their correspondence to. Both postal and email addresses match those that Mr H has provided in his complaint to this service, so I'm satisfied that HL accurately addressed their correspondence to the correct places. And, I think on balance, it's more likely than not that Mr H received that correspondence because he definitely received HL's letters at the start of their relationship highlighting the need to switch the original Bank B CTF as cash and then the subsequent November 2016 report.

But, in any event, even if Mr H didn't receive any emails or investment updates, the absence of such documents over a prolonged period of time should have put Mr H on a path of discovery that something wasn't right and prompted him to contact HL to understand what was happening with his daughter's plan. And as I've already explained, it was his responsibility and not HL's to continually monitor the ongoing appropriateness of the investments her monies were invested in.

Mr H said that he didn't think it was reasonable that HL should've put his daughter's monies in such a fund without having done their proper research. But, as I've already explained, the fund choice rested solely with him rather than HL. In light of the wider comments that Mr H has made about HL's promotion of the WEIF, I've considered whether HL's communications were clear, fair and not misleading and whether the relevant regulatory obligations that HL's communications needed to meet were actually met.

I understand Mr H's strength of feeling on the complaint and why he considers HL is responsible for the losses that his daughter has experienced on the WEIF. However, for the reasons I set out below, I'm not persuaded Mr H 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.

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 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 H'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 H 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 H 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 H to decide for themselves whether the risks and the features of the WEIF which HL was describing to them were right for their investment 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.

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 H 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 they 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 H and I understand why he feels HL ought to be responsible for the losses to his daughter's investment. But I'm satisfied that the financial loss Miss H experienced was not caused by something HL did or didn't do or because it misled Mr H 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 H's complaint that he's made on behalf of his daughter, and I won't be instructing Hargreaves Lansdown Asset Management Limited to take any further action.

Under the rules of the Financial Ombudsman Service, I'm required to ask Miss H to accept or reject my decision before 12 September 2024.

Simon Fox
Ombudsman