DRN-5005284

The complaint

Mrs B complains about investment advice she received from Hargreaves Lansdown Advisory Services Limited (HL). In particular, she complains about the advice it gave her to invest in two funds managed by Woodford because she says they weren't suitable for a cautious novice investor like her.

What happened

In October 2017 Mrs B approached HL for advice about investing some of her pension funds and other cash in order to provide an income for the future. In essence, maintenance payments she was receiving were due to end in the near future and she required advice to help make-up a future income shortfall of around £640 per month.

At the time Mrs B's had existing pension investments, some shares and cash ISAs (as well as some fixed interest investments). She described herself has having a "better than average" understanding in financial products, but saw herself as "naturally very cautious" when it came to investment risk. In her meeting with the adviser she explained however that given her upcoming income shortfall, she understood she needed to "take some risk to have the potential for capital growth". In describing her ideal asset allocation, Mrs B agreed she wanted a broad split of 15-25% fixed interest and 75-85% managed equities for her pension. And she wanted 25-35% fixed interest and 65-75% managed equities in her existing non-pension investment pot.

The adviser therefore recommended a broad portfolio of managed funds for both Mrs B's pension and non-pension money. These portfolios reflected the above asset allocation and included a recommendation to invest 8.3% in the Woodford Equity Income Fund (WEIF) as part of her pension, and 10.4% in the Woodford Income Focus Fund (WIFF) as part of her other portfolio.

In April 2020 Mrs B complained. She said, in short, that it was unfair that HL had recommended she invest in the WEIF and the WIFF and that at the time of the advice, HL ought to have known these funds weren't right for her. She asked for compensation.

HL looked into her complaint but didn't agree it had done anything wrong. It explained why it felt the investment advice she had received was suitable and why the WIFF and the WEIF were recommended as part of a broader portfolio of funds. It explained why it had continued to believe these investments were worthwhile investments and how it reached its conclusions.

Mrs B remained unhappy and referred her complaint to this service. One of our investigators looked into her complaint and concluded it should be upheld. In short, she thought that the portfolios that were recommended to Mrs B were outside her attitude to risk and weren't suitable for her.

Mrs B agreed but HL did not. It said:

- The investigator had given insufficient weight to what Mrs B had told the adviser and the discussions which were had between them – including the fact that Mrs B explained that she understood she needed to take more risk in order to achieve her objectives and understood that there was a shift in the risk she was taking with these assets following the advice. In relation to her pension, it was clear that Mrs B had not been happy with the growth and future prospects of her existing assets, and was therefore happy to transfer away in order to achieve potentially greater growth.

- HL therefore said that Mrs B was fully aware of the risks and was prepared to accept them in order to achieve her objectives.

- Furthermore, there was evidence of detailed discussions with Mrs B about what would happen in the event of high risks materialising, for example drops in value or market crashes.

- Mrs B told the adviser that given her long term horizon (13 years plus for her pensions), she was "quite comfortable" with dramatic drops in value. In terms of market crashes, she said she would "do nothing and wait for it to recover" and she was "comfortable accepting volatility". She confirmed that she didn't think her lifestyle would be impacted by a drop in her investments.

- This showed that Mrs B both accepted and understood the risks associated with the adviser's recommendations, so HL didn't agree that Mrs B had insufficient investment experience and knowledge to justify the risks of the investments she was recommended.

- It didn't agree with the investigator's method for putting things right.

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

I issued a provisional decision in August 2024. In it I said:

"*It's important to explain that my role in deciding Mrs B's complaint isn't to replace my view of what advice should've given to her at the time with the advice HL actually gave her. My role is to determine whether, taking into account the relevant rules, law and established good practice, as well as Mrs B's particular circumstances, it was fair and reasonable for HL to conclude, as it did, that its recommendations were suitable for her.*

In doing so, I should also make clear that each case this service looks at is decided on its own merits. This service doesn't operate on precedent like the courts. So whilst HL has pointed to other assessments by the service, I do not agree it is fair and reasonable to rely on those – they concerned different consumers, with different complaints and different personal circumstances. One "medium" risk investor is likely different to another, and it's therefore entirely possible for that same set of investments to be right for one but not another.

Mrs B's original complaint was centred very much on the two Woodford funds which she was recommended. I understand why – the WEIF was suspended and then liquidated in 2019, only a few years after her investment, likely causing her a substantial loss on that portion of her portfolio and the WIFF also suffered significant underperformance from 2018 onwards.

Although I've considered her comments about why she thinks the adviser shouldn't have *recommended either investment, I'm not persuaded by her comments for a number of reasons.*

I've seen insufficient evidence that there was an inherent reason which meant the WEIF and the WIFF were unsuitable for her. Mrs B's portfolio, as I go on to explain below, contained a mixture of UK and overseas equities – and both the WEIF and the WIFF were aligned with that. Whilst the WEIF, in 2017, contained some illiquid investments and a higher proportion of small cap companies than some of the other managed equities HL recommended, half of it was also still invested in large and mega cap UK companies – and it only formed a small portion of her pension portfolio. Whilst it was underperforming at the time of the advice, I don't consider that alone a sufficient reason to conclude that it was inherently unsuitable for Mrs B.

The WIFF, on the other hand, did not have any unlisted companies and was predominantly invested in UK equities. It had only been launched a few months prior. This means that both these funds had a place in Mrs B's portfolio, as long as the amount invested in them wasn't disproportionate. I say this because it is entirely acceptable for a portfolio of investments to have a mix of investments which represent a higher or lower risk than a consumer is willing to take, as long as the overall portfolio remains suitable for that consumer. In this case, I don't consider the WEIF and the WIFF were inherently unsuitable or that they represented a higher risk than Mrs B was willing to take at the time – but even if I did, I don't consider the amounts HL recommended Mrs B invest in them meant that her portfolios were unsuitable as a result.

However, notwithstanding the above, I don't consider it would be fair and reasonable to look at the recommendations to invest in the WEIF and the WIFF in isolation or to conclude that the entirety of the advice HL gave to her was unsuitable because these two funds underperformed. Both these investments were recommended to her in the context of a broader portfolio that had specific aims and objectives, and which was constructed by HL to meet what it considered were Mrs B's objectives and needs for her money.

So although Mrs B's complaint was initially about these investments, I have taken a step back and looked at Mrs B's portfolios overall, taking into account her discussions with the adviser, the suitability report, the fact find and Mrs B's complaint. It's important to note that I'm satisfied the evidence shows that Mrs B accepted in her conversations with the adviser that there were risks with the approach they were taking and that these risks could mean some capital losses. HL still had an obligation to consider whether taking these risks were suitable for her – but it is relevant to consider Mrs B's acceptance of these risks when looking at the advice she was given.

In looking at the recommendations HL provided, I've taken into account the fact that Mrs B had some clear and very well-defined needs. She had identified an upcoming income shortfall, which she was looking to bridge by investing her money (which had recently included an inheritance of £188,000), and she was keen to ensure a minimum level of income during her retirement – for which her existing arrangements appeared unsuitable. She described this income level as "essential".

In order to ensure that its recommendations were suitable, HL had to take into account Mrs B's financial objectives, as well as her attitude to investment risk and her overall financial circumstances. The regulator hasn't set out in a prescriptive way how firms ought to weigh up these considerations and so it's for individual firms to decide, based on everything they know about a customer, what investments best align with they're being told is required.

In my view, it was fair and reasonable for HL to consider that a higher proportion of managed equities was required for Mrs B to achieve her financial objectives – bearing in mind her long term time horizon and her overall financial circumstances. And I think, given the discussions it had with Mrs B, that it was fair and reasonable for it to conclude that bridging the income shortfall was of paramount importance to Mrs B – to the extent that she was able, and willing, to take additional risk in pursuit of that objective.

Furthermore, I'm satisfied that HL, in this particular case, was very clear about what Mrs B needed to do in order to achieve her objective. I've seen evidence that HL discussed risk with Mrs B in order to ensure she was comfortable with the amount of risk it was proposing to her. It's clear to me that during the fact find as well as in the suitability report, HL discussed in detail the fact that Mrs B was moving away from largely non-volatile assets to far more equity exposure – and that this was necessary to achieve the income needs she was describing. So I'm persuaded it was fair and reasonable for HL to conclude that the overall level of risk that it was recommending Mrs B take with her money was suitable for her and in line with her attitude to risk.

It's also important to note that the liquid assets Mrs B invested were not her only liquid assets. She had agreed to retain £25,000 on deposit for emergencies – and maintained a further £230,000 in cash through fixed deposits, building societies and cash ISAs. This is what led HL to conclude that Mrs B had the capacity to deal with potential losses – but I consider this was also a material consideration in the advice it gave her to invest in the various assets it considered suitable for her. I say this because this information shows Mrs B already had a large exposure to cash-based assets – and so I'm satisfied that it was therefore fair and reasonable for HL to conclude that a higher equity exposure in the portfolios Mrs B had asked to be advised on was suitable for her.

In looking through the various funds that it recommended, I'm also satisfied that they were broadly in line with what HL described to Mrs B as part of the advice process. The majority of her investments were in large or mega cap companies, with a focus on well established markets like the UK, the EU, the USA and Japan. The bond funds all contained predominantly government bonds of mainstream governments (mainly UK and USA) and investment grade corporate bonds. In other words, whilst these investments all caried varying level of risks, I'm satisfied HL had tried to strike a balance between Mrs B's needs to generate capital growth and income, while at the same time not be exposed to excessive volatility – given her background and what she had previously invested in.

Finally, I've considered whether Mrs B had sufficient knowledge to understand the additional risks HL was recommending she taken with her assets. I'm persuaded she did and that it was reasonable for HL to conclude that she did. In my view, whilst Mrs B wasn't an experienced investor, she knew and understood the reasons why she was being recommended investments which carried greater risks than the ones she already had.

It's clear that she understood the relationship between risk and reward in investing and further understood the impact of investing over the long term in order to be able to ride out market crashes or significant drops in value. All of these factors were discussed with Mrs B in such a way as to make it clear that she both understood and accepted these additional risks.

Taking everything into account, I'm currently persuaded that it was fair and reasonable for HL to conclude that the investments it recommended to Mrs B were suitable in light of her financial objectives, attitude to risk and overall financial circumstances. I fully appreciate that the performance of the WEIF and the WIFF would've likely impacted the overall performance of her portfolios in the short term, but the time horizon for Mrs B's investments was long term – and she had accepted that in some cases it was best to "wait out" crashes in the market *rather than reacting to them."*

HL and Mrs B's response to my provisional decision

HL didn't respond to my provisional decision. Mrs B provided detailed and comments and didn't agree she'd been given suitable advice. In summary, she said:

- She had never complained about the whole portfolio, but specifically about the inclusion of the Woodford funds;

- She'd decided to use HL because it claimed to "carry out continuous high-quality research and monitoring" of funds. She said that HL was aware of an increase in the proportion of small and unquoted assets and met with Woodford to discuss this.

- The WEIF was not just underperforming at the time of advice, it had been identified as problematic and therefore she said it wasn't appropriate to recommend it for inclusion of her portfolio. She said there were other funds in the HL Wealth 150 that could have been selected.

- HL trains its advisors to structure and record client interviews in a way that protects them against future challenges. She said that before she met with the advisor she didn't have specific figures that she wanted for ongoing income or for her pension – the objectives were recorded and proposed by the advisor.

- She had an inheritance she wanted to use to provide some income and she had existing pensions that she wanted reviewed and potentially consolidated, but she didn't have any target levels of income. Mrs B said she understood that funds carried more risk than fixed interest and that investments could rise and fall, so she did expect some volatility. She said she also understood that funds grew over time and therefore "waiting for recovery" was a sensible strategy, but she said that Woodford was not "conforming to accepted standards and was already failing at the time of HL's recommendation to invest".

- I had formed the view that it wasn't unreasonable to include Woodford funds in the total asset mix, but I had ignored the fact that there were other funds available that could have been included that did not carry the "higher than usual risks that had been identified with the situation Woodford was in at the time". Mrs B said that she therefore did not receive a suitable recommendation.

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 taken into account Mrs B's comments. But for the reasons I set out below and those that I set out in my provisional decision, I'm not persuaded her complaint should be upheld.

I've first set out the relevant standards that applied in 2017 and then explained my findings in relation to Mrs B's complaint.

Relevant standards

At the time of HL's advice, the Financial Conduct Authority (FCA) set out the rules in relation to investment advice in section 9 of its Conduct for Business Rules (COBS).

COBS 9.2 on Assessing Suitability said:

(1) A firm must take reasonable steps to ensure that a personal recommendation, or a decision to trade, is suitable for its client.

(2) When making the personal recommendation or managing his investments, the firm must obtain the necessary information regarding the client's:

  (a) Knowledge and experience in the investment field relevant to the specific type of designated investment or service;

  (b) financial situation; and

  (c) investment objectives;

so as to enable the firm to make the recommendation, or take the decision, which is suitable for him.

It then explained, at COBS 9.2.2, the type of information that would inform the above recommendation:

(1) A firm must obtain from the client such information as is necessary for the firm to understand the essential facts about him and have a reasonable basis for believing, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of managing:

  (a) meets his investment objectives;

  (b) is such that he is able financially to bear any related investment risks consistent with his investment objectives; and

  (c) is such that he has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.

(2) The information regarding the investment objectives of a client must include, where relevant, information on the length of time for which he wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.

(3) The information regarding the financial situation of a client must include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.

<u>My findings</u>

I'd like to reassure Mrs B that I understood her complaint. But as I explained in my provisional decision, my role is to look at HL's recommendations overall and decide whether it was fair and reasonable for it to conclude that they were suitable for her.

It isn't in my view fair and reasonable to look at the WEIF and the WIFF in isolation, without taking into account the rest of her portfolio. It is acceptable for a portfolio of investments to have a mix of investments which represent a higher or lower risk than a consumer is willing to take, as long as the overall portfolio remains suitable for that consumer. This is why I focused on the whole portfolio.

In relation to Mrs B's specific comments on the Woodford funds, I'm not persuaded that these funds were inherently unsuitable for her or for "any investor". The fact that the WEIF began increasing its exposure to small or unquoted assets meant that as a fund it was exposed to higher risk assets than it had been when it was launched, but this didn't make it unsuitable for everyone or meant that everyone who bought units in the fund was mis-sold them. In addition, as I explained in my provisional decision, at the time of the recommendation the WEIF was predominantly invested in large or mega cap UK companies – and given that she had limited exposure to this fund overall, I don't consider that the presence of the WEIF made her portfolio overall unsuitable or too risky for her.

I'm not sure what Mrs B means by the WEIF being "problematic", however I agree that there were other funds which could also have been recommended and would have been equally suitable. However, the adviser at the time didn't have the benefit of hindsight – and as I've said, my role isn't to replace his decision to recommend certain investments with my own. The adviser was required to use his judgement to select a combination of investments that, overall, would be suitable for her – given her attitude to risk, her financial circumstances and her objectives. I'm not persuaded there was anything about either the WIFF or the WEIF that meant that the adviser should not have considered those funds at all at the time of the advice. The subsequent performance of those funds isn't something that I consider relevant to the adviser's actions at the time of the advice.

Whilst I've fully considered Mrs B's comments about the WEIF and the WIFF, I remain of the view that it was fair and reasonable for HL to have recommended these funds, as part of a broader portfolio.

In terms of Mrs B's comments about the way HL recorded the information from her fact find, I understand the point that she has made, and I've given due consideration to her testimony. However, I've also placed weighed on the contemporaneous evidence available to me. Whilst Mrs B may not have had a specific target level of income in mind, given the information she disclosed to the adviser, it was fair and reasonable for them to consider the income shortfall and come up with a strategy to bridge it. If this was not a priority for Mrs B, in my view it was for her to make it clear to the adviser that protection of her capital was more important than making up the income shortfall she had disclosed. In my view, even if I accept that HL had come up with the specific income figures, it's more likely than not that Mrs B had a need and an objective to generate an income from this investment and it was fair and reasonable for the adviser to take this into account when coming up with their recommendations.

Furthermore, I'm also satisfied that the fact Mrs B continued to hold significant other cash based assets was also a relevant consideration for the adviser when coming up with these recommendations. I remain of the view that it was therefore fair and reasonable for HL to conclude that a higher equity exposure in the portfolios Mrs B had asked to be advised on was suitable for her.

I acknowledge the losses Mrs B sustained on these funds were disappointing and with hindsight, she would've been better off with other investments. But I'm not persuaded it would be fair and reasonable to uphold her complaint with the benefit of hindsight – and I'm satisfied the losses she sustained were caused by market movements which, unfortunately, are a risk when making equity based investments.

For these reasons and those that I gave in my provisional decision (and which I also confirm here as final), I'm persuaded HL acted fairly and reasonably and I don't uphold Mrs B's complaint.

My final decision

My final decision is that I don't uphold Mrs B's complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs B to accept or reject my decision before 10 October 2024.

Alessandro Pulzone
Ombudsman