DRN-4390225

The complaint

Mr M complains that Deep Blue Financial Limited (Deep Blue) arranged the transfer of his pension to a Self-Invested Personal Pension Plan (SIPP) and investment into unlisted shares causing him financial losses. He wants compensation for the losses incurred.

Both Mr M and Deep Blue are represented in this complaint by legal advisers, but I will just refer to Mr M and Deep Blue except where necessary.

What happened

Mr M says he attended some seminars about property investment. He was subsequently contacted by one of the presenters. About making an investment in an unlisted property development company called Forte Bailey (FB). FB's strategy was to purchase and redevelop residential sites in Southeast England. It targeted a five-year return of 100% (15% per annum). Mr M says he was then introduced to Deep Blue, an independent financial adviser, by a director of FB.

In December 2011 Deep Blue advised Mr M to transfer his existing personal pension plan with Standard Life to a SIPP with a pension provider called James Hay, to facilitate investment in FB. Around £37,000 was transferred. Deep Blue charged 5% upfront and 1% annual commission, which were deducted from the SIPP. James Hay then said it wasn't prepared to make in investment into FB. So, Deep Blue arranged a second transfer in May 2012 to a SIPP with Rowanmoor.

Shortly after £33,000 was invested in FB shares with a cash reserve held in the SIPP to cover future charges. Unfortunately, FB didn't generate the returns hoped for and experienced financial difficulties. It was placed into administration in July 2022 without providing any return to Mr M. His legal adviser says that no residual value is expected to be available.

Mr M's adviser complained to Deep Blue on 20 February 2023. It said the transfer to the SIPP had been wholly unsuitable advice. It raised multiple points including:

- Deep Blue failed to undertake a full fact find and hadn't established Mr M's financial position, and the investment comprised a significant proportion of his capital and all of his pension assets,
- It hadn't undertaken any meaningful comparison with his original pension plan reflecting the full costs involved, which were excessive,
- The investment was *"highly risky and illiquid"*, and inadequate due diligence had been carried out and he should have been advised not to proceed,
- The investment was only for *"sophisticated and experienced investors"*, which he wasn't,
- Whilst he knew he might not make a profit; he hadn't understood that he could lose all his capital.

Deep Blue said it didn't need to consider the complaint as it had been made too late. It said it was both more than six years since he took the SIPP out and three years since Mr M reasonably should have known he had grounds to complain. It said he knew FB wasn't performing as hoped and had raised queries about this on several occasions before. Including contacting an FB director in June 2019, which should have prompted him to consider the advice by then, at the latest.

Deep Blue also said the complaint was without merit. It said Mr M had completed a fact find form and written on it that he understood FB was "*a high risk investment*" that *"could also result in a total loss"*. It said a suitability report had been provided, setting out his *"Adventurous"* attitude to investment risk. And he'd wanted investments his current plan didn't offer and had already decided to proceed with FB. Which, if it did fail *"would have very little impact on your overall retirement plan"*. It said Mr M hoped to make good returns but understood that he could lose some or all of his capital.

Mr M referred his complaint to our service. Our investigator said we could consider it.

He said Mr M had called Deep Blue in November 2015 and made multiple complaints about the performance of FB, and the high charges on the SIPP, which he said hadn't been disclosed. And he'd questioned what was being provided for the fees. Our investigator said the complaints were made within six years of Mr M taking the SIPP out. But they hadn't been addressed by Deep Blue then. So, our service could now consider them.

Deep Blue disagreed. It said Mr M had been provided with full information in 2011. It said the issues raised in November 2015 were complaints about FB. It said the comments made by Mr M during the call didn't meet the definition of a complaint as it didn't amount *"to an allegation that* (Deep Blue's) *activities had caused him a financial loss, material distress or material inconvenience"*. It said whilst Mr M had referred to charges, he also said that he wouldn't have minded these if the investment *"had been performing well."* And this showed any complaint was about investment performance, which it wasn't responsible for. And Mr M's delay in making his complaint was *"incredible"*.

Our investigator said Deep Blue should have treated the November 2015 call as a complaint. As several of Mr M's comments related directly to it and were clearly complaints. Had it done so this would have given him referral rights to our service.

Our investigator considered the complaint itself and said it should be upheld.

He said Deep Blue was required to consider the suitability of underlying investment with FB. And if it didn't understand the investment or it wasn't suitable for Mr M it shouldn't have advised on the SIPP transfer, because it wasn't possible to assess the overall suitability of the advice. He said the Financial Conduct Authority had issued an alert in April 2014 reminding Firms of this existing requirement.

Our investigator said whilst Mr M might have said he was a sophisticated and experienced investor prepared to invest in high risk, illiquid investments that might be lost completely, this wasn't the case. As he had no experience of this type of investment. And was investing his entire pension fund, which he had no capacity to lose. That made the advice to transfer to the SIPP unsuitable and Deep Blue should have advised Mr M not to proceed. He said it should undertake calculations to establish the value of Mr M's previous pension plan had he not transferred and if this was higher than the value of the SIPP, it should compensate him accordingly.

Deep Blue disagreed. It said our investigator shouldn't have upheld the complaint until an ombudsman had decided whether it had been brought in time. Because it hadn't provided all its evidence and comments about the complaint itself. Our investigator said he'd reviewed the suitability letter, the fact find, attitude to risk questionnaire and FB prospectus in coming to his view, which he considered adequate evidence. He said if Deep Blue wished to submit any further evidence or comments it could do so. He asked that this be provided by 18 September 2023, this was extended twice, to 3 October 2023 and 1 November 2023. But Deep Blue didn't reply further.

As Deep Blue doesn't agree it has come 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.

Having done so I've decided that our service can consider this complaint and that it should be upheld.

If our service considers a complaint is within our jurisdiction, we can directly consider whether it should be upheld or not, without first issuing a decision on jurisdiction. This saves time and is in keeping with our remit to provide an informal and quick dispute resolution service. If the complaint is then referred for an ombudsman decision, the jurisdiction issue is considered first. And if I didn't think this complaint was within our jurisdiction, I would issue a decision saying that, and wouldn't consider the merits of the complaint at all.

Deep Blue didn't provide further comments but having considered the evidence I thought that some relevant information might be missing. So, I asked both Deep Blue and Mr M a number of questions about what happened.

Can I consider the complaint

Both Mr M and Deep Blue are familiar with the time limits applying as to whether a complaint can be made, so I won't set these out in full here. But briefly, a complaint can be made within either six years of the event complained about, or, if later, within three years of when the person ought reasonably to have been aware they had grounds to bring a complaint. Mr M received advice in December 2011 and further relevant advice in May 2012.

So, I think Mr M had until May 2018 to make a complaint under the first part of the rule. And I think he did make a complaint in his call to Deep Blue of November 2015, which was clearly inside the six-year timeframe. Making a complaint "stops the clock" in terms of the time limits applying. There is evidence Mr M complained then because the call was recorded. Deep Blue should have considered the complaint and provided a final response either accepting or rejecting it, giving Mr M six months from then to refer it to our service for an independent review.

Why I think Mr M complained in November 2015

Having listened to the call it is clear that Mr M made multiple complaints about how the investment was performing and the high administration costs being taken by both the SIPP provider and Deep Blue. Rowanmoor had recently written to him requesting that he pay £2,000 into the SIPP to cover future charges. He said he was out of work at the time and didn't have money for this. He described the charges as *"horrendous"* and an *"absolute rip off".* He referred to all concerned as *"sharks and cowboys".* He asked for an explanation of why the charges were so high, what he was getting for them and that these hadn't been explained to him. Deep Blue said it wasn't involved in the FB investment and vaguely explained the charges were for *"administration"*.

The regulator defines a complaint as being:

> ‘*any oral or written expression of dissatisfaction, whether justified or not, from, or on behalf of, a person about the provision of, or failure to provide, a financial service’*

Mr M made many, very clear expressions of dissatisfaction during the call. Deep Blue disputes that he went on to make any allegation it had caused him a *“financial loss, material distress or material inconvenience”,* as also set out in the complaint rules. But I disagree. Mr M was clearly very concerned about the charges being excessive and the impact these were having on him. That is clearly material distress and inconvenience and very obviously a potential financial loss due to those charges. There was no requirement for him to provide a fully formed argument and schedule of loss as if bringing legal proceedings.

So, I’m satisfied Mr M made a complaint in November 2015. That was within six years of him being advised to take out either SIPP, stopping the clock on the time limit to bring a complaint, so we can consider it.

Was the advice suitable

I don’t think it was suitable, and on many levels.

In giving advice to transfer Mr M’s Standard Life PPP to a SIPP Deep Blue was required to consider the whole position, not just the parts it wanted to. That meant it had to consider the appropriateness of the underlying investment in FB. So, I think this confusingly worded statement in its suitability report of May 2012 is wrong:

> *“I have explained to you that whilst we are unable to advise on the suitability of this specific investment (its likely performance and outcomes). I have advised that you must undertake your own due diligence in respect of this specific company, which you have confirmed to me you have done. However, we do consider if this type of investment is suitable for you, which I confirm that we do.”*

It is difficult to see how Deep Blue could reasonably say something was suitable if it couldn’t advise on it. But as it did say this, I think Mr M concluded it was advising him to proceed, despite the caveats about high risk, liquidity and so on. But it had a clear regulatory requirement to consider the suitability of the underlying investment. Having confirmed it didn’t do this, Deep Blue can’t demonstrate the advice was suitable for Mr M. That means the investment was mis-sold. Whilst I think this alone is sufficient for me to uphold his complaint, there are multiple other shortcomings. I’ll set out just a few specific examples of this below.

To consider whether the investment in FB was suitable Deep Blue needed to drill down into both it and the Mr M’s circumstances, his understanding of financial matters and his financial position. It needed to consider the costs involved and the impact these would have on any prospective return. And If the FB investment was outside its expertise, it should have declined to act for Mr M.

I asked Mr M about the discussions and meetings he had with Deep Blue. He says he doesn’t recall any face-to-face meetings. He thinks there was a telephone conversation and various documents were sent to him to sign. He says the handwriting on the fact find and attitude to risk (ATR) questionnaire isn’t his own and disputes some of the information entered is attributable to him. He points out that on the fact find his address is incorrectly entered, a mistake I agree he was unlikely to make himself. He also says he didn’t personally know FB’s directors as claimed in the suitability report.

The FB investment

FB was a high-risk investment, unsuitable for most investors. Saying that doesn't require the benefit of hindsight. According to its "*Share Offer Proposal"* document (the proposal), it was a start-up venture, seeking to raise a relatively small amount in investment terms of £2,000,000 capital and up to a further 60% in loans. And acquire properties between £400,000 to £600,000, to redevelop and resell within 9-12 months for between £800,000 to £1,300,000 over a five-year period before winding up and distributing profits to investors. Even if it raised £2,000,000, FB would clearly only be able (at least initially) to work on a few projects at a time, concentrating risk. It raised around £1,400,000, mostly from SIPP investors. The planned borrowing, whilst potentially boosting returns, also increased risk. And the lenders would have secured any loans against the property owned.

The proposal makes references to the director's successful track record. But there are inconsistencies, with this referred to as being over seven years then over nine years. With the number of deals ranging from *"over 50"* to *"60".* There are typing errors, like *"incentive"* being misspelt, ironically, as *"inventive"* in the financial outlook.

Initial costs were high. Estimated at £120,000 if £2,000,000 was raised. They included "*Marketing, Promotional and 3rd Party Fees"* of up to 5% of the equity raised, including undisclosed *"introducers fees".* Although Deep Blue says it didn't receive any payment from FB. A further £192,000 in operations and management costs were forecast in year one. There would be 2% per annum in *"Investor Relations fees"*, payable to a business owned by the directors. Whether these were included in the operation and management costs isn't clear. There was also a *"Performance and Incentive fee … of 20% of the assets of the company, calculated after the shareholders have received an annual return of 7% on their investments"*. This was payable to the director's other business. So, the impact of fees and charges would be considerable. And the calculations in the financial forecast don't appear to show the correct *"incentive fee",* which appears significantly understated.

Inconsistencies and errors like these should have been fairly obvious further red flags to a financial adviser considering the already very high-risk nature of the investment.

Mr M's capacity for loss

If FB could be considered a suitable investment for anyone it would only be for the most aggressive and wealthy investor with a clear capacity to carry a total loss. Yet Deep Blue made no record of Mr M's outgoings or whether he had other investments. Information that might have supported the contention that he was both a sophisticated and experienced investor, which with respect to him, I don't think he was. He had no experience of direct property investment and held no other investments.

When he complained in November 2015, Mr M said he hadn't been aware his capital was at risk, saying he thought the investment was asset backed by property holdings. When the advice was given, he was 50 years old, with an income of £30,000 and no other pension savings. That suggested he was dependent on those pension funds, with minimal capacity for loss. The fact find says he planned to grow his business and make other property investments. But Mr M says he never said his business could grow, because as a one-man design consultancy, it had no capacity to do so.

Even if Mr M did say all the things recorded on the fact find and ATR questionnaire (and I doubt he did) Deep Blue should have challenged these inconsistencies. Particularly his capacity for investment loss and either recommended suitable alternatives or told him it couldn't advise him. The suitability report from May 2012 does mention collective investments like unit trusts, saying Mr M would decide once the transfer was complete. But the report is very much written on the basis the FB investment was proceeding, advising that cash must be left in the SIPP to cover at least five years fees *"during the term of your Unlisted Share investment"* (FB).

Mr M's attitude to risk

Closely linked to capacity for loss is attitude to risk (ATR). Deep Blue assessed Mr M's ATR as being four out of five – *"aggressive"*. But inconsistently the appendix of the suitability report sets out nine categories of risk, with *"aggressive"* being eighth, defined as:

> *"You would like to maximise long term returns and are, not concerned by short term volatility, but still wish your short-term financial security to be provided by low risk investments"*

It isn't clear to me how the FB investment, a small, expensive, unregulated, illiquid, highly geared, and opaque venture operating in the notoriously risky property development sector, could provide any short-term financial security. Only the highest classification of risk used by Deep Blue (*"Speculative"*) mentioned any "*exposure to high-risk investments despite the potential loss of capital*". But even this definition required that "*your short and long-term financial security should still not be jeopardised."*

So, it's difficult to see how Deep Blue could have considered FB to be a suitable investment for the entirety of Mr M's pension funds if its own maximum categorisation of risk required both short and long-term financial security "*not to be jeopardised"*. On the ATR assessed alone, I think it should have advised Mr M not to proceed with the FB investment.

Charges

The charges with FB were high and needed to be considered by Deep Blue. The SIPP also came with relatively high charges. Mr M specifically complained about charges when he called it in November 2015. The suitability reports note the charges but don't put them into any context by explaining the impact they would have on the potential return. This is an important consideration for any investment. And unlike future performance it is a straightforward matter to accurately forecast the impact of charges.

SIPP providers often charge a monetary amount, rather than being percentage based. That means costs can be disproportionally high for a relatively small pension fund like Mr M's. Deep Blue initially recommended James Hay, whose total annual charges were over £900. This was around 2.67% of Mr M's net fund. And there was a further 1% annual charge from Deep Blue. That meant annual ongoing costs of at least 3.67%. The position improved somewhat as Rowanmoor charged less than James Hay. But ongoing costs were still high at around 2.6% per annum. This was in addition to the underlying costs in FB. With Deep Blue's 5% initial charge added, its and the SIPP's cumulative costs would equate to around 25% of the hoped for 15% annual return on the FB investment. Had James Hay been prepared to hold the FB investment these charges would have been around 32% of this hoped for return.

And crucially these charges would be incurred whether FB provided positive returns or not. The impact of these ongoing charges meant that Mr M could lose more than he'd actually invested. A high-risk strategy and high fixed charges are clearly a toxic combination for any investment in all but the most positive of outcomes. I think Deep Blue should have cautioned against the impact of the very high charges, but it did not.

I've also considered what Deep Blue's ongoing charges were for. This was a question Mr M asked repeatedly when he called in November 2015. The May 2012 suitability report says these included the following, with my emphasis in bold:

"Our Annual Adviser Fee specifically covers the ongoing administration ***and any further required advice connected to the SIPP****. It may include but is not restricted to;*

- *Administration of the SIPP including processing of any permissible investments.*
- *Routine record keeping and general technical and administration queries.*
- *Advice on the day to day running of the SIPP, …*

Further advice requirements should be directed to your specific adviser XX*, in the first instance."*

Given the above I think it is clear that Deep Blue had undertaken to provide ongoing advice. That should have included advice about FB as the underlying investment. So, when it told Mr M it wasn't responsible for the FB investment in November 2015, I don't think that was accurate. He specifically complained about Deep Blue's charges and asked what could be done. He was told that was up to the individual adviser and the question would be referred to him. There's no evidence that it was. And I see no reason why Mr M shouldn't have been told he could have declined ongoing services from Deep Blue and cancelled this charge if he wanted to. By not telling him that, it further failed to treat him fairly.

So, in terms of suitability, Deep Blue should have considered the underlying investment, it didn't. It should have considered Mr M's overall position and capacity for investment loss, it didn't or disregarded this. It should have advised him the risks applicable to the FB were much higher than his assessed ATR, it didn't. It should have advised him that the total costs of investing in FB through a SIPP were very high and explained the detrimental impact this would have even if investment returns were positive. Which meant a lower risk investment with much lower charges – like his existing pension plan - might offer better actual returns even if the headline return achieved was lower. It didn't do this.

So, I don't think Deep Blue treated Mr M fairly. The advice to proceed with the transfer to a SIPP and invest in FB was clearly unsuitable. And it appears that this has caused Mr M financial losses.

Putting things right

My aim in awarding compensation is to put Mr M back in the position he would have been in but for the unsuitable advice.

Fair compensation

I think it is reasonable that Mr M should have been advised to remain in his existing Standard Life pension plan, however I cannot be certain that a value will be obtainable for what the previous policy would have been worth. I am satisfied what I have set out below is fair and reasonable, taking this into account and given Mr M's circumstances and objectives when he invested.

What must Deep Blue do

To compensate Mr M fairly Deep Blue must:

- Compare the performance of Mr M's investment with the notional value if it had remained with the previous provider. If the actual value is greater than the notional value, no compensation is payable. If the notional value is greater than the actual value, there is a loss and compensation is payable.

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

- If there is a loss, Deep Blue should pay into Mr M's pension plan, to increase its value by the amount of the compensation and any interest. The payment should allow for the effect of charges and any available tax relief. It shouldn't pay the compensation into the pension plan if it would conflict with any existing protection or allowance.

- If Deep Blue are unable to pay the compensation into Mr M's pension plan, it should pay that amount direct to him. But had it been possible to pay into the plan, it would have provided a taxable income. Therefore, the compensation should be reduced to notionally allow for any income tax that would otherwise have been paid. This is an adjustment to ensure the compensation is a fair amount – it isn't a payment of tax to HMRC, so Mr M won't be able to reclaim any of the reduction after compensation is paid.

- The notional allowance should be calculated using Mr M's actual or expected marginal rate of tax at his selected retirement age.

- It's reasonable to assume that Mr M is likely to be a basic rate taxpayer at the selected retirement age, so the reduction would equal 20%. However, as Mr M would have been able to take a tax free lump sum, the reduction should be applied to 75% of the compensation, resulting in an overall reduction of 15%.

- Deep Blue should provide the details of the calculation to Mr M in a clear, simple format.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Rowanmoor SIPP	Still exists but illiquid	Notional value from previous provider	Date of transfer to James Hay SIPP	Date of settlement	Not applicable

Actual value

This means the actual amount payable from the investment at the end date.
If, at the end date, any investment in the portfolio is illiquid (meaning it cannot be readily sold on the open market), it may be difficult to find the actual value of the portfolio. So, Deep Blue should take ownership of any illiquid investments within the portfolio by paying a commercial value acceptable to the pension provider. The amount Deep Blue pays should be included in the actual value before compensation is calculated.

If Deep Blue is unable to purchase any illiquid investment the value of that investment should be assumed to be nil when arriving at the actual value of the portfolio. It may wish to require that Mr M provides an undertaking to pay it any amount he may receive from that investment in the future. The undertaking must allow for any tax and charges that would be incurred on drawing the receipt from the pension plan. It will need to meet any costs in drawing up the undertaking.

Notional Value

This is the value of Mr M's investment had it remained with the previous provider until the end date. Deep Blue should request that the previous provider calculate this value.

Any additional sum paid into the Rowanmoor SIPP should be added to the notional value calculation from the point in time when it was actually paid in.

Any withdrawal from the Rowanmoor SIPP to Mr M should be deducted from the notional 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 Deep Blue total all those payments and deduct that figure at the end to determine the notional value instead of deducting periodically.

If the previous provider is unable to calculate a notional value, Deep Blue will need to determine a fair value for Mr M's investment instead, using this benchmark: FTSE UK Private Investors Income Total Return Index. The adjustments above also apply to the calculation of a fair value using the benchmark, which is then used instead of the notional value in the calculation of compensation.

The Rowanmoor SIPP only exists because of illiquid assets. In order for the Rowanmoor SIPP to be closed and further fees that are charged to be prevented, those investments need to be removed. I've set out above how this might be achieved by Deep Blue taking over the portfolio, or this is something that Mr M can discuss with the provider directly. But I don't know how long that will take.

Third parties are involved, and I don't have the power to tell them what to do. If Deep Blue are unable to purchase the portfolio, to provide certainty to all parties I think it's fair that it pay Mr M an upfront lump sum equivalent to five years' worth of wrapper fees (calculated using the fee in the previous year to date). This should provide a reasonable period for the parties to arrange for the Rowanmoor SIPP to be closed.

Why is this remedy suitable

I've chosen this method of compensation because:

- Mr M wanted Capital growth and was willing to accept some investment risk.

- If the previous provider is unable to calculate a notional value, then I consider the measure below is appropriate.

- The start date used relates to the initial transfer from Standard Life to James Hay, so as to take account of the initial advice fee that was deducted at that time.

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

- Although it is called income index, the mix and diversification provided within the index is close enough to allow me to use it as a reasonable measure of comparison given Mr M's circumstances and risk attitude.

My final decision

My final decision is that I uphold the complaint against Deep Blue Financial Limited.

I direct Deep Blue Financial Limited to calculate and pay compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 27 December 2023.

Nigel Bracken
Ombudsman