DRN-3270930

The complaint

Ms M complains about the advice given by Quilter Financial Services Ltd to transfer the benefits from her defined-benefit ('DB') occupational pension scheme to a self-invested personal pension ('SIPP'). She says the advice was unsuitable for her.

Ms M is being represented by a third party but for ease of reading this decision I'll largely refer to representations as being made by Ms M.

What happened

Ms M was referred to an appointed representative of Quilter in late 2019 to discuss her pension and retirement needs.

Quilter completed a fact-find to gather information about Ms M's circumstances and objectives. It recorded that Ms M was 63, divorced, with two grown children, neither of which were financially dependent on her. She owned her own home and one of her children lived with her, with their family.

Ms M had a mortgage with an outstanding balance of approximately £30,000 as well as unsecured debts totalling around £13,500. She was paying £936 per month towards her mortgage and other debts.

Ms M had recently stopped working to provide care for her mother and did not intend to return to work. She wasn't in receipt of any pension income or state benefits at that time so her only income was £450 per month which her son, who lived with her, paid as rent or a contribution towards bills. She'd been paying her outgoings from savings, but these had now largely been exhausted with only approximately £1,000 remaining.

Quilter noted that Ms M expected to need an income of approximately £1,000 per month in retirement. And it says she was interested in accessing her pension benefits now, using tax-free cash ('TFC') to pay off her debts and complete some work to her home and drawing an income to cover her income needs, with her state pension entitlement then contributing towards these from age 66.

Quilter recorded that Ms M had a DB pension from the employer she'd recently left. The pension benefits had a cash equivalent transfer value ('CETV') of £222,950.61. The scheduled retirement age for her DB pension was 66, at which point it would provide a guaranteed income of either £12,531 per year with TFC of £17,447, or a reduced annual pension of £8,990 and TFC of £59,936.

Quilter also carried out an assessment of Ms M's attitude to risk, which it deemed to be 'moderate'.

On 28 November 2019, Quilter advised Ms M to transfer her pension benefits away from her DB scheme, take the maximum available TFC and invest the remainder into a SIPP (with 99.75% in a 'Moderate Passive portfolio' and the remaining 0.25% in 'cash'). The suitability report said the reasons for this recommendation were that it would provide the maximum available TFC to repay her liabilities and complete her home renovations. The new pension would provide her flexibility to draw a higher amount initially to cover her income needs and then reduce this when she began receiving state pension. It also allowed for the value of the pension to be passed to her children in the event of her death, which was Ms M's preference.

The transfer went ahead in line with the recommendation.

Ms M complained in March 2021 to Quilter about the suitability of the transfer advice. She said she hadn't understood, and it hadn't been explained to her, that she was giving up valuable guaranteed benefits by transferring and replacing these with higher risk alternatives. She said she was an inexperienced investor with a conservative attitude to risk. And the amount of TFC received was virtually the same as she could've taken from her existing scheme. So, she felt she was worse off and that the advice was unsuitable.

Quilter didn't uphold Ms M's complaint. It said it felt the advice was suitable in her circumstances. Quilter said the recommended pension had provided a TFC sum that covered her debts, gave her the flexibility of taking her pension in a way that suited her plans and provided more suitable death benefits in relation to her circumstances.

Ms M referred her complaint to our service. An Investigator upheld the complaint and required Quilter to pay compensation. In summary she felt the need for some of the things Quilter said that the recommendation provided – flexibility and death benefits - had been overstated. And she felt Ms M could've met her needs by remaining in her existing scheme and either waiting until her scheduled retirement date or taking her benefits straight away. She also thought Ms M was always going to be worse off as a result of the transfer, which she believed Quilter hadn't emphasised sufficiently. So, she didn't think the recommendation was in Ms M's best interests.

Quilter disagreed. It said it felt the Investigator had placed too much emphasis on the difference in the pensionable income and not thought about what was right for Ms M. It said that the existing scheme wouldn't have allowed Ms M to meet her needs, which it considered to be urgent. And the other benefits of transferring were appropriate for Ms M's circumstances and in line with preferences she had expressed.

The investigator wasn't persuaded to change their opinion, so the complaint was referred to me to make a final decision.

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'd like to reassure both parties that I've carefully considered all the evidence provided. If I don't comment on or refer to everything I've been sent this isn't meant as a discourtesy or because I haven't thought about it. Rather it is because my decision will address what I consider to be the key issues in deciding what is fair and reasonable.

I've taken into account relevant law and regulations, regulator's rules, guidance and standards and codes of practice, and what I consider to have been good industry practice at the time. This includes the Principles for Business (PRIN) and the Conduct of Business Sourcebook ('COBS'). And where the evidence is incomplete, inconclusive or contradictory, I reach my conclusions on the balance of probabilities – that is, what I think is more likely than not to have happened based on the available evidence and the wider surrounding circumstances.

The applicable rules, regulations and requirements

The below is not a comprehensive list of the rules and regulations which applied at the time of the advice but provides useful context for my assessment of Quilter's actions here.

PRIN 6: *A firm must pay due regard to the interests of its customers and treat them fairly.*

PRIN 7: *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.*

COBS 2.1.1R: *A firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule).*

The provisions in COBS 9 which deal with the obligations when giving a personal recommendation and assessing suitability. And the provisions in COBS 19 which specifically relate to a DB pension transfer.

Having considered all of this and the evidence in this case, I've decided to uphold the complaint for largely the same reasons as the investigator.

The regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.16 that the starting assumption for a transfer from a DB scheme is that it is unsuitable. So, Quilter should have only considered a transfer if it could clearly demonstrate that the transfer was in Ms M's best interests. And having looked at all the evidence available, I'm not satisfied it was in her best interests.

Financial viability

As part of the process of giving its recommendation, Quilter instructed a transfer analysis to help assess if the transfer was appropriate. This gave an indication of the likelihood of Ms M being able to match or exceed the benefits offered by her existing pension if she transferred.

The analysis included calculating a transfer value comparator ('TVC'). This is a comparison of the CETV of the existing pension and the estimated cost of Ms M achieving the same benefits that the DB scheme guaranteed in an alternative pension. Ms M's CETV was £222,950.61. But to achieve the same income that the DB scheme offered it was estimated she'd need to pay £420,361.88. So, the same benefits would cost her £197,411.27 more if she transferred.

The analysis also included the calculation of a critical yield ('CY') – the annual growth rate required of a new pension to enable Ms M to purchase equivalent benefits to those due under the DB scheme at retirement, at age 66. This was calculated as being 29.36% if Ms M took the full pension under her DB scheme or 20.15% if she took TFC and a reduced pension at retirement.

The advice was given after the regulator gave instructions in Final Guidance FG17/9 as to how businesses could calculate future 'discount rates' in loss assessments where a complaint about a past pension transfer was being upheld. Prior to October 2017 similar rates were published by the Financial Ombudsman Service on our website. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, they provide a useful indication of what growth rates would have been considered reasonably achievable for a typical investor.

The relevant discount rate closest to when the advice was given which I can refer to was published by the Financial Ombudsman Service for the period before 1 October 2017 and was 2.7% per year for two years to retirement. I’ve kept in mind that the regulator's projection rates had also remained unchanged since 2014: the regulator's upper projection rate at the time was 8%, the middle projection rate 5%, and the lower projection rate 2%.

I've taken this into account, along with the composition of assets in the discount rate, the ‘moderate’ attitude to risk Quilter recorded Ms M as having and also the term to retirement. And I’ve also thought about what the TVC said about how much equivalent benefits would cost. And having done so, I think Ms M was likely to receive benefits of a substantially lower overall value than the DB scheme at retirement, as a result of transferring and investing in line with that attitude to risk. So, from a financial viability perspective, the transfer wasn’t in Ms M’s best interests.

Of course, financial viability isn’t the only consideration when giving transfer advice. And Quilter has argued that the Investigator overstated the importance of this and that the transfer was suitable and in Ms M’s best interests, because it allowed her to meet important objectives, despite providing overall lower benefits.

The main purpose of a pension is though to provide benefits in retirement to the pension holder. And given, as I’ve set out, the transfer meant Ms M was always likely to receive overall benefits of a substantially lower value, I do consider this to be important. I have though thought carefully about the other reasons for transferring Quilter has mentioned.

Flexibility and income needs

Quilter has said that Ms M needed to take TFC immediately to clear her debts (totalling £43,500) and that she intended to use the residual funds to carry out some home improvements. And it says Ms M needed flexibility regarding her income. It says she had agreed she needed an income of £12,000 per year. So, she required more income from her pension between the point of advice and age 66 – while she was not earning – with her then being able to reduce how much she was drawing from this pension when her state pension became payable. So, it thinks the recommendation was in her best interests as Ms M’s needs could not have been met through her existing scheme.

I haven’t seen anything that suggests Ms M was in arrears with any of her debts. But it hasn’t been disputed that Ms M had left work to provide care for her mother and so her income had dramatically decreased. And I think it is reasonable to assume, given what was recorded about her income, that while she may’ve been up to date with payments at the point of the advice, she may’ve begun struggling with repayments in the short term. And given her financial situation, I think she likely did have an imminent need to clear her outstanding debt. I also don’t see any reason to question the income Ms M said she expected to need in retirement. But, as I’ll explain, I don’t agree this means she needed to transfer her pension or that doing so was in her best interests.

Ms M’s need was for £43,500 to clear debts. She said she intended to use the remainder for home improvements. But I don’t think the need for these home improvements was as pressing. And no set figure was recorded as being required for this purpose – Quilter simply indicated that Ms M would use whatever was left from her TFC.

I’ve seen a copy of the retirement options information from her existing DB scheme. And this indicates that, because Ms M was already 63, she could’ve taken a TFC sum of £52,930.59 from her existing DB scheme at the time of Quilter’s advice. And she could’ve also begun to draw a guaranteed annual pension of £7,939.60 – which would’ve continued to escalate in retirement. These figures were briefly mentioned in the suitability report. But were downplayed on the basis that the income would cease on Ms M’s death. But I don’t think this was appropriate.

The TFC sum available immediately from the DB scheme would've met Ms M's immediate needs of clearing her debt. And still provided a residual amount to make home improvements. While this was a slightly smaller than the residual amount of TFC that would've been available after transferring, I haven't seen anything to suggest it wouldn't have been enough to address Ms M's other objectives. And taking this benefit from the DB scheme would've meant that Ms M still received a guaranteed escalating pension for her lifetime.

The annual pension available from the scheme at that point was less than the £12,000 she expected to need in retirement. But again, it escalated and was guaranteed. And when combined with the £5,400 she was receiving per year from her son would've been enough to meet her income needs until her state pension entitlement began. And then when the state pension became payable, would've meant she comfortably received what she needed – more in fact. And the income was guaranteed, for her lifetime. She wouldn't have been required to reduce this just to ensure that the pension pot didn't run out – as she may've had to do under the scheme recommended. And although she may've ended up receiving more than she needed, that isn't necessarily a bad thing, and certainly is in my view preferable to taking unnecessary risk that her pension pot could run out.

Taking all of this into account, I don't think Ms M required flexibility in retirement. I'm satisfied she could have met her immediate needs and her income needs in retirement through the DB scheme at the point of the advice. I don't think this was made clear to Ms M. And, I don't think recommending that she transfer to achieve the same objectives, thus exposing her pension to investment risk and particularly bearing in mind what I've said about financial viability, was in her best interests.

Death benefits

Quilter said that by transferring Ms M was able to leave her entire remaining pension fund to her sons – which was her preference as she was divorced. So transferring was again in her interests as it achieved this goal. But in response to our Investigator's opinion it said this was a secondary objective so wasn't as significant a factor in the advice.

The suitability report said that Quilter considered this to be a *"compelling reason in favour of a transfer"*. So, contrary to what it has now said, I think it did place emphasis and weight on this point.

Death benefits are an emotive subject and of course when asked, most people would like their loved ones to be taken care of when they die. The lump sum death benefits on offer through a personal pension was likely an attractive feature to Ms M. But whilst I appreciate death benefits are important to consumers, and Ms M might have thought it was a good idea to transfer her DB scheme to a personal pension because of this, the priority here was to advise Ms M about what was best for her retirement provisions. A pension is primarily designed to provide income in retirement. She should not have been encouraged to prioritise the potential for higher death benefits through a personal pension over her security in retirement. And I don't think Quilter explored to what extent Ms M was prepared to accept a lower retirement income in exchange for higher death benefits.

In addition, the sum remaining on death under the SIPP would've been dependent on investment performance and would be reduced by any income Ms M drew. And if she had lived a long life the impact of this is likely to have been significant. The fact find recorded that she was in good health. And I've seen nothing to suggest her life expectancy was likely to be lower than normal. So, there may not actually have been a large sum left and the fund may have in fact been depleted, particularly if Ms M lived a long life.

And if Ms M genuinely wanted to leave a legacy for her children, which didn't depend on investment returns or how much of her pension fund remained on her death, I think Quilter should've instead explored life insurance.

Overall, I don't think different death benefits available through a transfer to a SIPP justified the likely decrease of retirement benefits for Ms M. And I don't think that insurance was properly explored as an alternative.

Suitability of investments

Quilter recommended that Ms M invest in a specific portfolio. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Ms M, it follows that I don't need to consider the suitability of the investment recommendation. This is because Ms M should have been advised to remain in the DB scheme and so the investments wouldn't have arisen if suitable advice had been given.

Summary

I don't doubt that the flexibility and death benefits on offer through a SIPP may've sounded like attractive features to Ms M. But Quilter's role was to really understand what Ms M needed and recommend what was in her best interests.

Ultimately, I don't think the advice given to Ms M was suitable. She was giving up a guaranteed, risk-free and increasing income, which she could've begun drawing immediately and which, alongside the tax-free cash available through her existing scheme and the payments she received from her son, would've allowed her to meet her needs. By transferring, Ms M was very likely, and indeed almost certain, to obtain lower retirement benefits and, in my view, there were no other particular reasons which would justify a transfer and outweigh this.

So, I think Quilter should've advised Ms M to remain in their DB scheme and begin drawing her benefits straight away.

Of course, I have to consider whether Ms M would've gone ahead anyway, against Quilter's advice.

I've considered this carefully, but I'm not persuaded that Ms M would've insisted on transferring out of the DB scheme, against Quilter's advice. I say this because Ms M was an inexperienced investor with a moderate attitude to risk and this pension accounted for the majority of her retirement provision. So, if Quilter had provided her with clear advice against transferring out of the DB scheme, explaining why it wasn't in her best interests, I think she would've accepted that advice.

I'm not persuaded that Ms M's concerns about her death benefits were so great that she would've insisted on the transfer knowing that a professional adviser, whose expertise she had sought, didn't think it was suitable for her or in her best interests. If Quilter had explained that Ms M could meet all of her objectives without risking her guaranteed pension, I think that would've carried significant weight. So, I don't think Ms M would have insisted on transferring out of the DB scheme.

In light of the above, I think Quilter should compensate Ms M for the unsuitable advice, using the regulator's defined benefits pension transfer redress methodology. Quilter has suggested it doesn't think this is fair as Ms M would've had the benefit of retiring early and then still be compensated as if she had remained in the DB scheme. But for the avoidance of doubt I think it should've recommended that she take her benefits straight away under the DB scheme. So, I think the regulator's redress methodology is still appropriate here – using that assumption.

Putting things right

A fair and reasonable outcome would be for Quilter to put Ms M, as far as possible, into the position she would now be in but for Quilter's unsuitable advice. I consider Ms M would have most likely remained in her DB scheme if suitable advice had been given.

On 2 August 2022, the FCA launched a consultation on new DB transfer redress guidance and has set out its proposals in a consultation document - CP22/15-calculating redress for non-compliant pension transfer advice. The consultation closed on 27 September 2022 with any changes expected to be implemented in early 2023.

In this consultation, the FCA has said that it considers that the current redress methodology in Finalised Guidance (FG) 17/9 (Guidance for firms on how to calculate redress for unsuitable defined benefit pension transfers) remains appropriate and fundamental changes are not necessary. However, its review has identified some areas where the FCA considers it could improve or clarify the methodology to ensure it continues to provide appropriate redress.

The FCA has said that it expects firms to continue to calculate and offer compensation to their customers using the existing guidance in FG 17/9 whilst the consultation takes place. But until changes take effect firms should give customers the option of waiting for their compensation to be calculated in line with any new rules and guidance that may come into force after the consultation has concluded.

We've previously asked Ms M whether she preferred any redress to be calculated now in line with current guidance or wait for any new guidance / rules to be published.

She has chosen not to wait for any new guidance to come into effect to settle her complaint.

I am satisfied that a calculation in line with FG17/9 remains appropriate and, if a loss is identified, will provide fair redress for Ms M.

Quilter must therefore undertake a redress calculation in line with the regulator's pension review guidance as updated by the Financial Conduct Authority in its Finalised Guidance 17/9: Guidance for firms on how to calculate redress for unsuitable DB pension transfers.

For clarity, I think if appropriate advice had been given Ms M would've taken benefits (the maximum available TFC and reduced pension) under her DB scheme at the point of the advice, when she was aged 63. So, this should be the basis for the calculations.

This calculation should be carried out as at the date of my final decision and using the most recent financial assumptions at the date of that decision. In accordance with the regulator's expectations, this should be undertaken or submitted to an appropriate provider promptly following receipt of notification of Ms M's acceptance of the decision.

Quilter may wish to contact the Department for Work and Pensions (DWP) to obtain Ms M's contribution history to the State Earnings Related Pension Scheme (SERPS or S2P). These details should then be used to include a 'SERPS adjustment' in the calculation, which will take into account the impact of leaving the occupational scheme on Ms M's SERPS/S2P entitlement.

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Ms M's SIPP. The payment should allow for the effect of charges and any available tax relief. The compensation shouldn't be paid into the pension plan if it would conflict with any existing protection or allowance.

If a payment into the pension isn't possible or has protection or allowance implications, it should be paid directly to Ms M as a lump sum after making a notional deduction to allow for income tax that would otherwise have been paid. Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to her likely income tax rate in retirement - presumed to be 20%. So, making a notional deduction of 15% overall from the loss adequately reflects this.

The payment resulting from all the steps above is the 'compensation amount'. This amount must where possible be paid to Ms M within 90 days of the date Quilter receives notification of her acceptance of my final decision. Further interest must be added to the compensation amount at the rate of 8% per year simple from the date of my final decision to the date of settlement for any time, in excess of 90 days, that it takes Quilter to pay Ms M.

It's possible that data gathering for a SERPS adjustment may mean that the actual time taken to settle goes beyond the 90 day period allowed for settlement above - and so any period of time where the only outstanding item required to undertake the calculation is data from DWP may be added to the 90 day period in which interest won't apply.

If the complaint hasn't been settled in full and final settlement by the time any new guidance or rules come into effect, I'd expect Quilter to carry out a calculation in line with the updated rules and/or guidance in any event.

Where I uphold a complaint, I can award fair compensation of up to £355,000, plus any interest and/or costs that I consider are appropriate. Where I consider that fair compensation requires payment of an amount that might exceed £355,000, I may recommend that the business pays the balance.

My final decision

Determination and money award: I uphold this complaint and require Quilter Financial Services Ltd to pay Ms M the compensation amount as set out in the steps above, up to a maximum of £355,000.

Where the compensation amount does not exceed £355,000, I would additionally require Quilter Financial Services Ltd to pay Ms M any interest on that amount in full, as set out above.

Where the compensation amount already exceeds £355,000, I would only require Quilter Financial Services Ltd to pay Ms M any interest as set out above on the sum of £355,000.

Recommendation: If the compensation amount exceeds £355,000, I also recommend that Quilter Financial Services Ltd pays Ms M the balance. I would additionally recommend any interest calculated as set out above on this balance to be paid to Ms M.

If Ms M accepts this decision, the money award becomes binding on Quilter Financial Services Ltd.

My recommendation would not be binding. Further, it's unlikely that Ms M can accept my decision and go to court to ask for the balance. Ms M may want to consider getting independent legal advice before deciding whether to accept any final decision.

Under the rules of the Financial Ombudsman Service, I’m required to ask Ms M to accept or reject my decision before 17 November 2022.

Ben Stoker
Ombudsman