DRN-3323921

Financial Ombudsman Service

The complaint

Mr M complains about the advice given by Portal Financial Services LLP ('Portal') to transfer the benefits from his preserved defined-benefit ('DB') occupational pension scheme to a personal pension arrangement. He says the advice was unsuitable for him and believes this has caused a financial loss.

What happened

In 2017 in response to an advert, Mr M approached Portal to discuss his pension and retirement needs.

Portal completed a fact-find during a telephone-based appointment to gather information about Mr M's circumstances and objectives. Portal also carried out an assessment of Mr M's attitude to risk, which it deemed to be 'moderately adventurous' – a score of 12 on a scale of 0-14.

In December 2017, Portal advised Mr M to transfer his pension benefits into a SIPP and invest the proceeds in an investment portfolio comprising three funds – a mix of equities, fixed-interest securities and cash. The suitability report set out the reasons for the recommendation, which can be summarised as:

- To provide Mr M with flexibility and a pension that could adapt to his changing needs and circumstances in the future;
- To maximise tax-free cash to meet Mr M's objective;
- To offer greater choice and flexibility of death benefits;
- To provide Mr M with ownership and control of his pension; and
- To provide the opportunity for growth through Mr M's willingness to take on investment risk.

In 2021 Mr M, through a representative, complained to Portal about the suitability of the transfer advice. He said he had no investment experience and questions why Portal recommended the transfer given this and because the critical yield required would be difficult to achieve given his attitude to risk. He says Portal should have refused to take on the business rather than going ahead and making a recommendation.

Portal didn't uphold Mr M's complaint. It sent Mr M an 18-page letter explaining its decision. I haven't repeated all of this here because both parties are aware of its contents.

But in summary it said that it considered Mr M's circumstances, his objectives for a lump sum for the purpose of home improvements and to reduce his outstanding mortgage and it made a suitable recommendation to transfer based on this having also considered the alternatives available to him. It said it believed there was a good chance of pension growth because it deemed the 'hurdle rate' could be exceeded given the past performance of the investments recommended. Overall it said Mr M had received suitable advice.

Mr M referred his complaint to our service. And investigator upheld the complaint and required Portal to pay compensation. In summary they said the critical yield required to match Mr M's benefits in his existing scheme was too high given the relevant discount rate at the time and given Mr M's attitude to risk – albeit they didn't think a moderately adventurous attitude to risk was an appropriate assessment of the risk they thought Mr M was willing to take. They disagreed with Portal's argument that the hurdle or growth rate of 3.6% was a more realistic measure of viability because they said there was no evidence that Mr M needed flexibility of income. And given it was his only source of income in retirement, they didn't think he'd want to risk giving it up.

They said that Mr M's objective of wanting to repay his mortgage couldn't happen because his mortgage was subject to a redemption penalty, something Portal hadn't considered in giving its advice. And because Mr M's home improvements cost less than the remaining sum of tax-free cash, he'd spent it on luxury items and put some in savings. They said if Portal had properly established Mr M's needs, it wouldn't have recommended he transfer, which they said Mr M would've likely accepted.

Portal disagreed. In doing so it repeated much of what it said in its final response letter to Mr M. Overall it said the advice was suitable because it met Mr M's documented objectives and because it believed the hurdle or growth rate was achievable given Mr M's desire for flexibility of income withdrawal. It said there were no viable alternatives available to Mr M and so a correct recommendation was made - Mr M has not been financially disadvantaged as a result of the transfer. Finally it disagreed with the investigator that it was for it to consider whether Mr M's mortgage had any redemption penalties – it says it assumed Mr M had investigated this himself and it was entitled to rely on the information Mr M provided as being accurate.

Because the investigator wasn't persuaded to change their opinion, the complaint was referred to me for 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.

When considering what is fair and reasonable, I am required to take into account relevant law and regulations; regulators' rules, guidance and standards; codes of practice; and, where appropriate, what I consider to have been good industry practice at the time.

Having done so, I've decided to uphold the complaint for largely the same reasons given by the investigator. My reasoning is set out below.

The regulator, the Financial Conduct Authority ('FCA'), states in its Conduct of Business Sourcebook ('COBS') that the starting assumption for a transfer from a DB scheme is that it is unsuitable.

So, Portal should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr M's best interests (COBS 19.1.6). And having looked at all the evidence available, I'm not satisfied it was in his best interests.

Financial viability

Portal says the advice to transfer out of Mr M's DB scheme was in his best interests – it says it was suitable and appropriate for his needs and circumstances.

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, I consider they provide a useful indication of what growth rates would have been considered reasonably achievable when the advice was given in this case.

The closest discount rate to the time of this transfer which I'm able to refer to was published for the period before 1 October 2017 and is 3.4% per year for seven years to retirement. The share returns that were used to compile this discount rate wouldn't have been significantly different by the time of transfer and, if anything, the bond returns would have got lower. So, I think it still gives an approximate guide to the upper end of potential future returns.

For further comparison, the regulator's upper projection rate at the time was 8%, the middle projection rate 5%, and the lower projection rate 2%.

The critical yield required to match Mr M's benefits at age 65 was 14.2% if he took a full pension and 11.8% if he took a tax-free lump sum and a reduced pension.

I've taken this into account, along with the composition of assets in the discount rate, Mr M's recorded attitude to risk as a 'moderately adventurous' and also the term to retirement.

In my view there would be little point in Mr M giving up the guarantees available to him through his DB scheme only to achieve, at best, the same level of benefits outside the scheme. But here, taking the most likely option of Mr M taking tax-free cash and a reduced pension, the critical yield was 11.8%. This figure was significantly higher than both the regulator's middle and upper projection rates – it was also more than three times higher than the discount rate. And while I have some concerns about how Portal arrived at classifying Mr M as a 'moderately adventurous' investor given his apparent lack of any real investment experience and the term to retirement, even if I thought this was the level of risk Mr M was prepared to take with his pension, I think it was clear he was likely to receive benefits of a substantially lower overall value than his DB scheme at retirement, as a result of investing in line with that attitude to risk.

Because the required sustained growth rate was more than three times the discount rate, I think it is clear the transfer was not compatible with Mr M's attitude to risk. To have come close to achieving the level of growth required, in my view would have required Mr M to take significant investment risk, which was far greater than his recorded appetite. And even then I think it's more likely than not that Mr M would have been worse off financially at retirement if he transferred out. I think the term to retirement was also a limiting factor here.

I can see Portal says the hurdle or growth rate is more appropriate in this case, which is what the adviser based their advice on. This is because Mr M said he preferred the idea of a flexible drawdown as opposed to an annuity to generate his pension income, which is what the critical yield figure assumes. It seems to me that Portal is implying the relevance of the critical yield figure was limited in this case.

But I don't think the importance of the critical yield figures should have been downplayed by the adviser, which I think is what happened here. The regulator required Portal to provide the rates of return required to replicate the benefits available to Mr M through his DB scheme.

So, telling Mr M it wasn't really relevant to him undermined the analysis the regulator required it to undertake. And I think given the high critical yield figures in Mr M's case, these should have acted as a clear sign that Mr M ought to retain his DB scheme and that transferring out was not likely to be in his best interests.

Overall, I think Portal ought to have told Mr M it wasn't in his best interests to transfer out of the DB scheme because I think it's clear that he would be worse off financially if he did so. And for this reason alone, I don't think the advice to transfer out was suitable. Of course financial viability isn't the only consideration when giving transfer advice. I accept there might be other considerations which mean a transfer is suitable, despite providing overall lower benefits. I've considered these below.

Flexibility – access to tax-free cash and income needs

Mr M's objective and the reason for the recommendation to transfer out of his DB scheme was to access his tax-free cash to make home improvements and to reduce his mortgage.

But I don't think this was a suitable reason to recommend the transfer. I say this because firstly and crucially in my view, the adviser did not establish how much money Mr M really needed to achieve his plans – it was simply based on him accessing the maximum tax-free cash based on the transfer value. From what I can see Mr M didn't need this amount of money - he told us the home improvements he made cost no more than £10,000. And as for repaying his mortgage, it turned out that Mr M couldn't do this because of an early redemption penalty – so he used the extra monies to purchase some luxury items and to add to his savings.

I think Portal should have better understood the details of Mr M's mortgage before it went ahead and made a recommendation for Mr M to transfer out of his DB pension scheme for the purpose of repaying his mortgage. Portal didn't know Mr M's outstanding mortgage balance or the terms of the mortgage - so importantly it didn't consider whether it was possible for Mr M to repay his mortgage early and whether early redemption penalties might apply. Portal says it assumed that Mr M would have checked this beforehand with his mortgage lender and says the rules permit it to rely on the information it's given by a client. But the information Portal had about Mr M's mortgage was incomplete – so I don't think it was in a position to make a suitable recommendation. At the very least I would've expected the adviser to have told Mr M to go away and check this information with his mortgage lender before recommending he go ahead with an irreversible decision to transfer out of his DB scheme. By not doing this and assuming that Mr M had already obtained this information was not, in my view acting in Mr M's best interests.

In any event, it's not clear to me why Mr M needed to repay his mortgage at this stage. Just because Mr M thought it was a good idea didn't mean Portal had to execute what he thought he needed – it was Portal's role to decide what was in his best interests. It's recorded that Mr M said his mortgage payment was manageable and I've not seen anything to suggest otherwise. In my view the mortgage was likely subject to a low rate of interest given interest rates had been at historic lows for some time.

And Mr M wasn't planning on retiring any time soon – so he could've continued to service the debt from his earned income. Given this, I'm not persuaded there was a need for Mr M to repay the debt at this stage and certainly no pressing need to access his tax-free cash earlier than his scheme's normal retirement age to achieve it. I see no reason why Mr M couldn't have waited and used his tax-free cash from his DB scheme at his normal retirement age if a balance remained outstanding on his mortgage at this time.

So on the basis that Mr M's only viable objective at the time was to access a lump sum for home improvements – and for an amount of no more than £10,000 - I would've expected the adviser to have properly explored the alternatives available to him. In my view a loan or further advance to his mortgage was a realistic possibility for Mr M. And while I can see the suitability report says lending was discussed but discounted by Mr M because he didn't want to take on further lending or pay any interest, I'm not persuaded these were fully considered given the lack of consideration for the amount of money Mr M truly needed.

I think greater emphasis should have been placed on this as a means to achieve Mr M's goal. Mr M had no other debts, interest rates were low at this time and given the poorly completed budget planner and lack of meaningful detail, I'm not persuaded it was reasonable for Portal to arrive at the conclusion that Mr M didn't have any disposable income he could've used to service a loan. I'm not persuaded that Mr M's objective couldn't have reasonably been met this way rather than recommending he make an irreversible decision to transfer his DB scheme to a personal arrangement to help achieve it.

The other reason Portal gave for the recommendation to transfer was to provide greater flexibility in how Mr M took future income – he didn't want to buy an annuity. But I can't see that Mr M had a strong, if any need for variable income through his retirement. Mr M's future income needs weren't known at the time – he had no plans to retire any time soon - so I don't know how he could've decided this. Furthermore, if Mr M did in fact have a need for flexibility in retirement, I think this could've been explored closer to his intended retirement age, which was still several years away.

Overall I'm not persuaded Mr M's need for flexibility was a real objective – I think it was simply a consequence of transferring out to a different arrangement to meet Mr M's need for access to cash.

Death benefits

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 arrangement was likely an attractive feature to Mr M. But whilst I appreciate death benefits are important to consumers, and Mr M might have thought it was a good idea to transfer his DB scheme to a personal pension arrangement because of this, the priority here was to advise Mr M about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think Portal established the extent to which Mr M was prepared to accept a lower retirement income in exchange for higher death benefits.

I also think the existing death benefits attached to the DB scheme were underplayed. Mr M was married - so the spouse's pension provided by the DB scheme would've been useful to his spouse if Mr M predeceased her. I don't think Portal made the value of this benefit clear enough to Mr M. This was guaranteed and it escalated – it was not dependent on investment performance, whereas the sum remaining on death in a personal pension was. In any event, Portal should not have encouraged Mr M to prioritise the potential for higher death benefits through a personal pension over his security in retirement.

While I'm mindful that Mr M was 57 at the time, if he genuinely wanted to leave a legacy for his spouse, which didn't depend on investment returns or how much of his pension fund remained on his death, I think Portal should've instead explored life insurance. This didn't have to be a whole of life policy with a sum assured for the full transfer value, which given Mr M's age might have been costly. The starting point ought to have been to ask Mr M how much he wanted to leave to his family, and this could've been explored on a whole of life or term assurance basis, which I consider was likely to be cheaper to provide.

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

Ownership and control

I think Mr M's documented desire for ownership and control over his pension benefits was overstated. Mr M was not an experienced investor and I've seen nothing to show or suggest that he had an interest in or the knowledge to be able to manage his pension funds on his own. So, I don't think that this was a genuine objective for Mr M – it was simply a consequence of transferring away from his DB scheme.

Summary

I don't doubt that the immediate availability of tax-free cash, flexibility, control and the potential for higher death benefits on offer through a personal pension arrangement would have sounded like attractive features to Mr M. But Portal wasn't there to just transact what Mr M might have thought he wanted. The adviser's role was to really understand what Mr M needed and recommend what was in his best interests.

Ultimately, I don't think the advice given to Mr M was suitable. He was giving up a guaranteed, risk-free and increasing income to meet one objective which turned out not to be viable and the other that in my view with better advice and consideration could likely have been achieved through other means such as a form of borrowing. And this would've been far preferable to Mr M giving up his only guaranteed retirement income. By transferring, Mr M was very likely to obtain lower retirement benefits and in my view, there were no compelling reasons which would justify a transfer and outweigh this.

So, I think Portal should've advised Mr M to remain in his DB scheme.

I now need to consider whether Mr M would've gone ahead anyway, against Portal's advice.

Having done so, I don't think Mr M would've insisted on transferring out of his DB scheme and gone head in any event. I say this because Mr M was not in my view an experienced investor, despite Portal's classification of his attitude to risk which might suggest otherwise. So I think he relied solely on the advice he was given. At the time this pension was the primary source of Mr M's guaranteed future retirement provision. So, if Portal had provided him with clear advice against transferring out of the DB scheme, explaining why it wasn't suitable for him, and if it had explained that Mr M should explore alternative sources of funding for his home improvement objective and not risk his guaranteed pension to do so, I think that would've carried significant weight. I think Mr M would've accepted that advice.

In light of the above, I think Portal should compensate Mr M for the unsuitable advice, using the regulator's defined benefits pension transfer redress methodology.

Putting things right

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

Portal 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.

My understanding is that Mr M could access the benefits from his pension scheme at 65. So, compensation should be based on his normal retirement age of 65, as per the usual assumptions in the FCA's guidance.

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 Mr M's acceptance of the decision.

Portal may wish to contact the Department for Work and Pensions (DWP) to obtain Mr 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 Mr M's SERPS/S2P entitlement.

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Mr M's pension plan. 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 Mr 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 his 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 Mr M within 90 days of the date Portal receives notification of his 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 Portal to pay Mr 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.

Where I uphold a complaint, I can award fair compensation of up to £160,000, 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 £160,000, I may recommend that the business pays the balance.

My final decision

<u>Determination and money award</u>: I uphold this complaint and require Portal Financial Services LLP to pay Mr M the compensation amount as set out in the steps above, up to a maximum of £160,000.

Where the compensation amount does not exceed £160,000, I would additionally require

Portal Financial Services LLP to pay Mr M any interest on that amount in full, as set out above.

Where the compensation amount already exceeds £160,000, I would only require Portal Financial Services LLP to pay Mr M any interest as set out above on the sum of £160,000.

Recommendation: If the compensation amount exceeds £160,000, I also recommend that Portal Financial Services LLP pays Mr M the balance. I would additionally recommend any interest calculated as set out above on this balance to be paid to Mr M.

If Mr M accepts this decision, the money award becomes binding on Portal Financial Services LLP.

My recommendation would not be binding. Further, it's unlikely that Mr M can accept my decision and go to court to ask for the balance. Mr 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 Mr M to accept or reject my decision before 16 August 2022.
Paul Featherstone
Ombudsman