DRN-3388875

The complaint

Mr H complains about the advice given by Esteem Money Ltd to transfer the benefits from his defined-benefit ('DB') occupational pension scheme to a personal pension. He says he was mis advised about moving his pension and the advice was unsuitable for him. He believes this has caused him a financial loss.

What happened

In March 2016, Mr H's employer announced that it would be examining options to restructure its business, including decoupling the BSPS (the employers' DB scheme) from the company. The consultation with members referred to possible outcomes regarding their preserved benefits, which included transferring the scheme to the Pension Protection Fund ('PPF'), or a new defined-benefit scheme ('BSPS2'). Alternatively, members were informed they could transfer their benefits to a private pension arrangement.

In May 2017, the Pension Protection Fund (PPF) made the announcement that the terms of a Regulated Apportionment Arrangement (RAA) had been agreed. That announcement said that, if risk-related qualifying conditions relating to funding and size could be satisfied, a new pension scheme sponsored by Mr H's employer would be set up – the BSPS2.

In October 2017, members of BSPS were being sent a "Time to Choose" letter which gave them the options to either stay in BSPS and move with it to the PPF, move to BSPS2 or transfer their BSPS benefits elsewhere. The deadline to make their choices was 11 December (and was later extended to 22 December 2017).

Mr H sought advice about his pension planning from another financial adviser. But this adviser couldn't give advice on Mr H's pension and so Mr H was referred to Esteem.

Mr H approached Esteem in November 2017 to discuss his pension and retirement needs. Esteem's notes about this early time show that Mr H contacted it due to concerns about, and a lack of trust with, his DB scheme.

Esteem completed a fact-find to gather information about Mr H's circumstances and objectives. This showed that he was:

- Aged 49, married and in good health.
- Employed by Tata Steel and earning around £37,000 a year. Mrs H was also employed with an income of £28,080.
- Mr H was a member of his employer's group personal pension scheme.
- He had a deferred money purchase pension fund that had a current value of around £50,000.
- Mr and Mrs H owned their own home which was subject to a mortgage of around £44,000. They had some other debts of about £6,000.
- Mr H had cash savings of £11,000, they had no other savings or investments.

Esteem also carried out an assessment of Mr H's attitude to risk, which it deemed to be 'high or moderately adventurous'.

On 19 November 2017, Esteem advised Mr H to transfer his pension benefits into a personal pension. The transfer proceeded and Mr H transferred £87,662.02 into a Liverpool Victoria personal pension that invested in a range of funds.

The suitability report said that Mr H's main aims for this pension were to:

- Clear all his debts.
- To retire early. He wanted to possibly begin to take benefits from his pension at age 55, and fully retire at age 60.
- Provide better lump sum death benefits for his wife and children.

Esteem said the new personal pension offered him the flexibility to do this, it said that the personal pension income benefits would be comparable to the DB scheme, and the death benefits would be greater. It would also alleviate Mr H's concerns with the funding of the scheme and his concerns about his employer. It said the transfer amount was good value.

Mr H complained in 2021 to Esteem about the suitability of the transfer advice. Mr H thought he might have been adversely affected by the transfer and he wanted to compare it to the BSPS benefits he gave up.

Esteem didn't uphold Mr H's complaint. It said the advice was suitable for him and would allow him to clear his debts and retire early. He needed a flexible pension solution which the BSPS2 or the PPF wouldn't offer. It said he didn't want to transfer to the BSPS2 and felt that his pension would end up in the PPF which would reduce his benefits.

Mr H referred his complaint to our service. An investigator upheld the complaint and recommended that Esteem pay compensation. He said that the transfer was likely to have left Mr H worse off in retirement. He said that even though the BSPS2 and PPF provided lower benefits than the BSPS they were still valuable. This wasn't properly explained to Mr H. And it wasn't properly demonstrated that transferring the DB scheme would meet his aims.

Esteem disagreed, saying:

- Whist the critical yields were high they were achievable given Mr H's attitude to risk.
- In any case Mr H wanted to use these funds flexibly and so the critical yields weren't entirely relevant.
- Mr H didn't want to take the risk of his employer's scheme having problems in the future.
- Mr H was fully aware of what the BSPS2 and PPF could offer him. The point of sale documentation explained this fully.
- Mr H might still need cash at 55 to repay debt and he may have downsized. Taking benefits in the way he wanted to was not available from his DB scheme.

There was some further correspondence after this, but the investigator wasn't persuaded to change their opinion. No new issues were raised. 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'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 rules below are 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 Esteem'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 given by the investigator.

The regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.6 that the starting assumption for a transfer from a DB scheme is that it is unsuitable. So, Esteem should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr H's best interests. And having looked at all the evidence available, I'm not satisfied it was in his best interests.

Financial viability

Esteem carried out a transfer value analysis report (TVAS), as required by the regulator, showing how much Mr H's pension fund would need to grow by each year in order to provide the same benefits as his DB scheme (the critical yield). However, this was based on his existing scheme benefits and Mr H didn't have the option to remain in the BSPS – he either needed to opt into the BSPS2 or move with the scheme to the PPF. The suitability report shows information about Mr H's entitlements from the BSPS2.

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.

Mr H was 49 at the time of the advice and wanted to retire at age 60, and earlier if possible. The critical yield required to match Mr H's benefits at age 60 from the BSPS2 was 9.45% The same figure at his age 65 was 7.56%.

The critical yield to match the benefits available through the PPF at age 60 was shown to be 8.27% if Mr H took full pension benefits and 7.91% if he took a reduced pension and tax-free cash.

The TVAS said that Mr H would need a fund of £222,964.34 to provide the same pension benefits as the BSPS at age 60. And if he took maximum tax-free cash this fell to £178.752.57.

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 was 3.8% per year to age 65, and 4.2% per year to age 60. 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%.

Esteem didn’t produce a full cashflow analysis, which would have been best practice and helpful here. But it did say that if Mr H took the same benefits as he could from the DB scheme then the fund would run out at his 78 if he took a full pension and 80 if he took a tax-free cash and a reduced pension. This was based on his retirement at age 60.

Mr H’s attitude to risk was assessed as being relatively high. I can accept he indicated that he was prepared to take some risk. But he also doesn’t seem to have had any risk bearing investments, so it’s hard to accept that he would be familiar with the volatility that investing at higher risks usually brings. And I don’t think he had any real capacity for loss given his pension funds were modest. Nevertheless, even if I accept that he was prepared to take some risk, the required returns are approaching, or above, the regulators highest growth rates and so were not likely to be achievable however he invested.

I've taken all of this into account, along with the composition of assets in the discount rate, Mr H's attitude to risk and also the term to retirement. I think it’s clear that Mr H was likely to receive benefits of a materially lower overall value than the occupational scheme at retirement, as a result of investing in line with his attitude to risk. This was especially the case if he retired early (as planned).

Esteem says that the critical yields are of limited relevance as Mr H didn’t want to use his funds on the same basis as the benefits provided by the DB scheme. Essentially Esteem is saying Mr H didn’t want an annuity, it said he wanted to take his benefits flexibly. But the regulator required Esteem to consider the rate of investment growth that would have to be achieved to replicate the benefits being given up. So, it needed to provide an analysis based on the critical yield and I do think it is a relevant consideration here, particularly as I don’t think Mr H wasn’t sure whether he would want to take a regular income at retirement from this pension. He wasn’t expecting to retire for at least another five to ten years. His only other pension was a money purchase arrangement, so that was already subject to investment risk. So, I think it’s entirely possible that Mr H would want at least some guaranteed income in retirement (which he could achieve by taking benefits from the DB scheme).

Esteem has questioned the use of the discount rate as a means of considering whether the critical yields were achievable. But under COBS 19.1.2 the regulator required businesses to compare the benefits likely to be paid under a DB scheme with those payable under a personal pension by using reasonable assumptions. So, businesses were free to use the discount rate as this would be considered a reasonable assumption of the likely returns. And in any event, this has been considered in tandem with the regulator’s published projection rates, which providers were required to refer to. And it is this combination, along with Mr H’s attitude to risk, which leads me to be believe he'd likely be worse off in retirement if he transferred out of the DB scheme.

For this reason alone, a transfer out of the DB scheme wasn't in Mr H's best interests. Of course, financial viability isn't the only consideration when giving transfer advice, as Esteem has said in this case. There might be other considerations which mean a transfer is suitable, despite providing overall lower benefits. I've considered these below.

Flexibility and income needs

It seems the main reason that Esteem recommended this transfer was for the flexibility and control it offered Mr H. But having considered the evidence, I don't think Mr H needed to transfer his DB scheme to a personal pension in order to have flexibility in retirement.

It's evident that Mr H could not take his DB scheme benefits flexibly. Although he could choose to take tax-free cash and a reduced annual pension, Mr H had to take those benefits at the same time. But I'm not persuaded that Mr H had any concrete need to take tax-free cash and defer taking his income, or to vary his income throughout retirement. To my mind this seems more of a 'nice to have' rather than a genuine objective.

There were two main objectives that this flexibility was intended to achieve. He firstly wanted to repay his debts between ages 55 and 60. And secondly, he wanted to retire at age 60 (or before).

Looking at the debt first, it was recorded that Mr and Mrs H's main borrowing was a mortgage which had a remaining amount of £44,000. They were repaying £1,240 a month to this arrangement, or around £15,000 a year. They were also covering all of their expenses including servicing their other debt of around £6,000 and saving on a regular basis. So, given the information recorded on the fact find, I think their debts would have been repaid within the next five years or so, if not earlier. Therefore, I don't think they needed to transfer for this reason. And I think Esteem ought to have known that paying down affordable debt is not a good enough reason to sacrifice guaranteed income required for retirement.

Turning to their income needs in retirement. According to the information gathered by Esteem Mr and Mrs H said they needed about £1,000 a month. The suitability report shows that Mr H was entitled to an annual income of £4,190 at age 60 from the BSPS2. He would get £4,140 from the PPF. The amounts at age 65 were £5,653 and £5,111.66 respectively. Mrs H had her own pension provisions and it's not clear how much this was. But it seems reasonable to say there may be a shortfall in their income needs at age 60, unless Mrs H's pension provided enough to top up what they needed.

Mr and Mrs H would also receive their state pensions in time. Which would cover further shortfalls at their state retirement ages.

The advice was given on the basis that the money from the DB transfer could be used flexibly to enable Mr H to retire early. But Mr H already had a sizable, flexible pension valued at £50,000 to draw on at retirement. And he was building up further funds in his employer's new scheme over the next six to ten years. He could use his DC scheme benefits to top up the income he would receive from DB scheme to meet his needs until the state pension became payable. Or he could use the lump sums for something else if this was not needed. So, I don't agree that the only way Mr H could meet his aims was to transfer his DB scheme.

I think the transfer reduced his flexibility as he could have used his DB scheme to provide a strong foundation for his income needs. This option is now not available to him. Mr H could also have waited until nearer the time and properly assessed how he could fund his early retirement if this is still what he wanted to do. And attempting to achieve his retirement objectives by transferring out of the scheme meant Mr H would be taking on all the investment risk, when he didn't need to.

As I've set out above, Mr H was unlikely to obtain benefits of the same value at retirement if he transferred his funds to a personal pension. So, I still think Mr H had a better chance of achieving his retirement aims by opting into the BSPS2 (the benefits under which were guaranteed and escalated) rather than relying on investment growth in a personal pension.

Overall, based on the evidence I've seen, I don't think Mr H had a genuine need to alter the arrangements he already had in place.

Death benefits

Providing lump sum death benefits was listed as one of Mr H's objectives but I can't see that he was given any detailed advice about this. It was recorded that he didn't have any dependents. He didn't have any children and his wife was employed and had her own pension provisions.

That said, 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 Mr H. But whilst I appreciate death benefits are important to consumers, and Mr H might have thought it was a good idea to transfer his DB scheme to a personal pension because of this, the priority here was to advise Mr H about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think Esteem explored to what extent Mr H was prepared to accept a lower retirement income in exchange for higher death benefits. It's not clear if any discussions about this went past the 'nice to have' stage.

I also think the existing death benefits attached to the DB scheme were underplayed. Mr H was married and so the spouse's pension provided by the DB scheme would've been useful to his spouse if Mr H predeceased him. I don't think Esteem made the value of this benefit clear enough to Mr H. This was guaranteed and it escalated – it was not dependent on investment performance, whereas the sum remaining on death in a personal pension was. And as the cashflow analysis shows, there may not have been a large sum left particularly if Mr H lived a long life. In any event, Esteem should not have encouraged Mr H to prioritise the potential for higher death benefits through a personal pension over his security in retirement.

Furthermore, if Mr H 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 Esteem should've instead explored life insurance. And Mr H could have nominated his wife as beneficiary of his other DC pension scheme.

Overall, I don't think different death benefits available through a transfer to a personal pension justified the likely decrease of retirement benefits for Mr H.

Control and concerns over financial stability of the DB scheme

It's clear that Mr H, like many employees of his company, was concerned about his pension. His employer had recently made the announcement about its plans for the scheme, and he was worried his pension would end up in the PPF. He'd clearly heard negative things about the PPF and he said he preferred to have control over his pension fund rather than his employer being involved in it.

So it's quite possible that Mr H was also leaning towards the decision to transfer because of the concerns he had about his employer and his negative perception of the PPF. However, it was Esteem's obligation to give Mr H an objective picture and recommend what was in his best interests.

As I've explained, by this point details of BSPS2 were known and it seemed likely it was going ahead. So, this should've alleviated Mr H's concerns about the scheme moving to the PPF.

But even if there was a chance the BSPS2 wouldn't go ahead, I think that Esteem should've reassured Mr H that the scheme moving to the PPF wasn't as concerning as he thought. The income available to Mr H through the PPF would've still provided a reasonable portion of the income he thought he needed at retirement, and he was unlikely to be able to exceed this by transferring out. And although the increases in payment in the PPF were lower, the income was still guaranteed and was not subject to any investment risk. And if Mr H took tax-free cash, it would've actually produced a better outcome for him. So, I don't think that these concerns should've led to Esteem recommending Mr H transfer out of the DB scheme altogether.

Suitability of investments

Esteem recommended that Mr H invest in a number of managed funds of varying risks. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Mr H, it follows that I don't need to consider the suitability of the investment recommendation. This is because Mr H should have been advised to remain in the DB scheme and so the investments in the Liverpool Victoria funds wouldn't have arisen if suitable advice had been given.

Summary

I don't doubt that the flexibility, control and potential for better death benefits on offer through a personal pension would have sounded like attractive features to Mr H. But Esteem wasn't there to just transact what Mr H might have thought he wanted. The adviser's role was to really understand what Mr H needed and recommend what was in his best interests.

Ultimately, I don't think the advice given to Mr H was suitable. He was giving up a guaranteed, risk-free and increasing income. By transferring, Mr H was very likely to obtain lower retirement benefits, and in my view, there were no other reasons which would justify a transfer and outweigh this. Mr H shouldn't have been advised to transfer out of the scheme just to repay debts that were affordable, and any concerns he had about his DB scheme or employer weren't worth giving up the guarantees associated with his DB scheme.

I appreciate that the BSPS2 hadn't been confirmed when the advice was given, but I think it was clear to all parties that it was likely to be going ahead. Mr H had around 10 years before he expected to retire, at the earliest, and his plans were not concrete.

So, I don't think that it would've been in his interest to accept the reduction in benefits he would've faced by the scheme entering the PPF, as it wouldn't be offset by the more favourable reduction for very early retirement. And by opting into the BSPS2, Mr H would've retained the ability to transfer out of the scheme nearer to his retirement age if he needed to.

Also, Mr H was married, and his wife's pension would be set at 50% of his pension at the date of death, and this would be calculated as if no lump sum was taken at retirement (if Mr H chose to do so). The annual indexation of his pension when in payment was also more advantageous under the BSPS2. So, I think Esteem should've advised Mr H to opt into the BSPS2.

Of course, I have to consider whether Mr H would've gone ahead anyway, against Esteem's advice.

I've considered this carefully, but I'm not persuaded that Mr H would've insisted on transferring out of the DB scheme, against Esteem's advice. I say this because I can't see that Mr H was an experienced investor and this pension was an important part of Mr H's retirement provision, I don't think he had capacity to lose it. So, if Esteem had provided him with clear advice against transferring out of the DB scheme, explaining why it wasn't in his best interests, I think he would've accepted that advice.

I'm not persuaded that Mr H's concerns about his employer and the scheme were so great that he would've insisted on the transfer knowing that a professional adviser, whose expertise he had sought out and was paying for, didn't think it was suitable for them or in his best interests. If Esteem had explained that Mr H could meet all of his objectives without risking his guaranteed pension, I think that would've carried significant weight. So, I don't think Mr H would have insisted on transferring out of the DB scheme.

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

Putting things right

On 2 August 2022, the FCA launched a consultation on new DB transfer redress guidance and set out its proposals in a consultation document - CP22/15-calculating redress for non-compliant pension transfer advice**.**

In this consultation, the FCA 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.

A policy statement was published on 28 November 2022 which set out the new rules and guidance-https://www.fca.org.uk/publication/policy/ps22-13.pdf. The new rules will come into effect on 1 April 2023.

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 for the time being. But until changes take effect firms should give customers the option of waiting for their compensation to be calculated in line with the new rules and guidance.

We've previously asked Mr H whether he preferred any redress to be calculated now in line with current guidance or wait for the new guidance/rules to come into effect.

Mr H would like his complaint to be settled in line with new guidance and or rules. So, I consider it's fair that Esteem calculates Mr H's redress in line with new guidance and rules when they come into effect.

A fair and reasonable outcome would be for the business to put Mr H, as far as possible, into the position he would now be in but for the unsuitable advice. I consider he would have opted into the BSPS2.

The basic objective of the amendments to the redress methodology still remains to put a consumer, as far as possible, into the position they would be in if the business had advised them to remain in the DB scheme. Having reviewed the FCA’s consultation and policy statement, I’m satisfied that the changes still reflect a fair way to compensate Mr H.

Esteem must undertake a redress calculation in line with the updated methodology as soon as any new rules and/or guidance come into effect (rather than to calculate and pay any due compensation now in line with FG17/9).

For clarity, Mr H has not yet retired, and he has no firm plans to do so at present. So, compensation should be based on his/her/their normal retirement age of 65, as per the usual assumptions in the FCA's guidance.

In accordance with the regulator’s expectations, this should be undertaken or submitted to an appropriate provider promptly once any new guidance/rules come into effect.

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Mr H’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 H 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 compensation amount must where possible be paid to Mr H within 90 days of the date any changes to DB transfer redress guidance or new rules come into effect and Esteem has received notification of Mr H’s acceptance of my decision. Further interest must be added to the compensation amount at the rate of 8% per year simple from the date any changes to DB transfer redress guidance or new rules come into effect to the date of settlement for any time, in excess of 90 days, that it takes Esteem to pay Mr H.

Income tax may be payable on any interest paid. If Esteem deducts income tax from the interest, it should tell

Mr H how much has been taken off. Esteem should give Mr H a tax deduction certificate in respect of interest if Mr H asks for one, so he can reclaim the tax on interest from HM Revenue & Customs if appropriate.

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

Determination and money award: I uphold this complaint and require Esteem Money Ltd to pay Mr H 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 Esteem Money Ltd to pay Mr H any interest on that amount in full, as set out above.

Where the compensation amount already exceeds £160,000, I would only require Esteem Money Ltd to pay Mr H any interest as set out above on the sum of £160,000.

Recommendation: If the compensation amount exceeds £160,000, I also recommend that Esteem Money Ltd pays Mr H the balance. I would additionally recommend any interest calculated as set out above on this balance to be paid to Mr H.

If Mr H accepts this decision, the money award becomes binding on Esteem Money Ltd .

My recommendation would not be binding. Further, it's unlikely that Mr H can accept my decision and go to court to ask for the balance. Mr H 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 H to accept or reject my decision before 13 January 2022.

Andy Burlinson
Ombudsman