DRN-3620137

Financial Ombudsman Service

The complaint

Mr E complained that he was given unsuitable advice to transfer his defined benefit (DB) British Steel Pension Scheme (BSPS), to a type of personal pension plan, in 2018.

Makemson & Company Limited is responsible for answering this complaint and so to keep things consistent, I'll refer mainly to "Makemson".

What happened

In March 2016, Mr E's employer announced that it would be examining options to restructure its business, including decoupling the BSPS 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 personal pension arrangement.

In May 2017, the 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 E's employer would be set up – the BSPS2.

In October 2017, members of the 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 2017 (and was later extended to 22 December 2017).

Mr E was concerned about what the announcement by his employer meant for the security of his preserved benefits in the BSPS. He was unsure what to do and was referred to Makemson which is responsible for providing the pension advice. Information gathered about his circumstances and objectives at the time of the recommendation were broadly as follows:

- Mr E was 55 years old and married. He was described as being in good health at the time.
- Mr and Mrs E lived in a home valued at around £112,000 with an outstanding mortgage of around £60,000.
- Mr E earned around £37,000. Mrs E also worked. After expenses they had some disposable income left over. Mr and Mrs E had joint savings of £77,000.
- The cash equivalent transfer value (CETV) of Mr E's BSPS was approximately £424,455. The normal retirement age (NRA) was 65 although Makemson said he had evidently expressed a desire to retire earlier, if possible, at the age of 57.
- Mr E had joined the new defined contribution TATA pension scheme as a consequence of BSPS closing to new contributions. This pension isn't the subject of

any complaint.

Makemson set out its advice in a suitability report on 9 January 2018. In this it advised Mr E to transfer out of the BSPS and invest the funds in a type of personal pension plan. Makemson said this would allow Mr E to achieve his objectives. Mr E accepted this advice and so transferred out. In 2022 Mr E complained to Makemson about its advice, saying he shouldn't have been advised to transfer out to a personal pension.

Mr E later referred his complaint to the Financial Ombudsman Service. One of our investigators looked into the complaint and said it should be upheld. They also said Mr E ought to be paid £300 for the distress and inconvenience this matter has caused him.

In response, Makemson said it hadn't done anything wrong and was acting on the financial objectives Mr E had at the time. However, Makemson has since said it would like to settle the complaint. It said it would do this in full and using a specific redress calculator which the financial regulator has established for these types of cases. So, Makemson asked for Mr E to supply details of his transferred pension value so it can begin the process of establishing if there has been a loss. Makemson said if there was a loss, then it will pay what is due under the guidelines issued by the financial regulator.

However, Mr E still hasn't agreed to supply the details Makemson has requested about his current pension value, so it can start off the calculation using the BSPS-calculator. This is because he doesn't think there has been a "no loss". He's asked for an ombudsman's final decision first. There's also a dispute about what factors should be used when using the calculator. For example, Mr E believes his original NRA of 65 years should be used in the calculation. And he also thinks the scheme he would have joined if he hadn't been given unsuitable advice was the BSPS2 scheme. On the other hand, Makemson says that Mr E is now known to have accessed his transferred pension earlier than the original NRA and so his stated intentions during the course of the advice sessions to 'retire' earlier than 65, have been borne out.

Therefore, even though I can see Makemson is apparently willing to settle this complaint using the general approach we endorse, this can't evidently be resolved informally. It's therefore come 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.

I've also 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 Businesses ('PRIN') and the Conduct of Business Sourcebook ('COBS'). 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 Makemson'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.

I have further considered that 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, Makemson should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr E's best interests.

I've used all this information we have to consider whether transferring away from the BSPS to a personal pension was in Mr E's best interests. I have also carefully considered the latest responses whereby Makemson is offering to use the redress methodology and approach that it implies the Financial Ombudsman Service endorses.

Having done all this, I'm upholding Mr E's complaint about the transfer advice being unsuitable. However, it is my decision that any redress calculation should be based on Mr E retiring at the NRA of 65, but from the PPF. I explain all this below.

<u>Introductory issues</u>

I've noticed a matter which I don't think has been raised by anyone else up until this point: it relates to the potential redress that could be due.

As I've said above, we know that BSPS members had until 22 December 2017 to make a decision about what they wanted to do - this was a 'hard' deadline. If the member didn't make a choice, then their only remaining options were to transfer away, or move to the PPF. If they missed the deadline for choosing, then moving into the BSPS2 had been lost and was therefore 'out of time'.

In this case, it does look as if Mr E only initially met with Makemson on 30 December 2017. This is confirmed by Makemson. This was already *after the deadline*. We also know the suitability report (recommending the transfer) was on 9 January 2018 (again - after the deadline). And as I'd seen nothing showing Mr E had previously made a choice to elect to join the BSPS2 before the deadline, I asked him about this. Mr E has confirmed there is nothing showing such a choice was ever made before 22 December 2017. So, because Makemson's dealings with Mr E all appear to be after the deadline, I can't hold Makemson responsible for not recommending he should move to the BSPS2. That's because by then, BSPS2 was no longer an option for him. This means Mr E's only remaining option (other than transferring) was to move to the PPF.

<u>Was the advice unsuitable?</u>

Because I understand Makemson has agreed to carry out a loss calculation, I therefore don't see the need to address the suitability of Makemson's advice to Mr E in the same detail as I would normally. However, to be clear, I fully agree with the investigator's view that the advice was unsuitable, and I do so using the same rationale.

Makemson's transfer advice was unsuitable for the following reasons:

- The critical yield is essentially the average annual investment return that would be required on the transfer value - from the time of advice until retirement - to provide the same annuity benefits as the DB scheme. In this case, Makemson used the BSPS even though this was no longer an option for Mr E. This was a shortcoming although our experience is that critical yields for the BSPS2 would be probably marginally lower – and lower again for the PPF.

- Nevertheless, it said the critical yield was 7.94% if retiring at the age of 65 with the BSPS and taking a tax-free lump sum. If retiring on the BSPS at 57 the critical yield was 34.74%. Conversely, the discount rates for the above scenarios were only 3.7% and 2.5% respectively (for around 10 years or 2 years to retirement). So, I think this was already showing that by transferring away from the DB scheme, Mr E was unlikely to be able to grow his pension to a degree which made transferring financially viable.

- I've kept in mind that the regulator's upper projection rate at the time was 8%, the middle projection rate was 5%, and the lower projection rate was 2%. But I've also considered the higher costs associated with a personal pension and that Mr E's limited knowledge of investing would have probably required ongoing support and management from a professional adviser. Everything I've seen shows – that when viewed from the point of advice in 2017 - he would likely receive lower pension benefits in the longer term as a result of transferring away from the DB scheme.

- Makemson applied an attitude to risk (ATR) categorisation that was set which was medium high (or 5/7). I think this was too high. Mr E may well have answered some questions on a form indicating a higher ATR, but the evidence here is that he had limited investment experience other than through his wife's share scheme through her job or his own other (DC) pension which had an 'off the shelf' investment strategy requiring no direct input from him.

- In my view, the rationale given for the transfer was poor. Like our Investigator, I also think the early retirement at the age of 57 was no more than an idea at the time. Mr E had no fixed plans for this and he should have been advised to stay within a DB type scheme until the decision about retiring was more certain.

- I've seen nothing explaining why Mr E wouldn't want to continue membership of a DB scheme and to use that scheme in exactly the way it was originally intended. Indeed, I think that by retirement, whenever it eventually came, Mr E could have been in an agreeable position. On one hand he'd have an existing deferred DB scheme of considerable value. This would contain all the guarantees and benefits that such schemes normally bring which tend to include a promise to pay a known pension for life. Significant indexation guarantees still existed, even within the PPF. On the other hand, he had another pension; although this was still relatively small, he'd have built up more as time went by. Both he and his employer were making substantial contributions every month. So, if Mr E ever found he needed so-called flexibility, then he'd be able to use the latter, rather than transferring away from the former. He also had significant savings.

- I've also seen no evidence that Mr E had either the capacity or desire to exercise control over his funds. What I've seen tends to show Mr E would have required ongoing financial advice and support, all of which would cost him money which his DB scheme didn't require from him.

- Death benefits - the PPF contained certain benefits payable to a spouse and children if Mr E died. Mr E was married so I think the value of these benefits were most likely underplayed because the spouse's pension provided by the PPF would have been useful to Mrs E if he predeceased her. I don't think Makemson made the value of this benefit clear enough. This was guaranteed and it escalated – it was not dependent on investment performance, whereas the sum remaining on death in a personal pension was.

- I think the adviser told Mr E that he'd be able to pass on the whole value of a personal pension, potentially tax-free, to anyone that he nominated. So the lump sum death benefits on offer through a personal pension were probably made to look like an attractive feature to Mr E. But this needed carefully explaining. Whilst I appreciate death benefits are important to consumers, and Mr E might have thought it was a good idea to transfer the BSPS to a personal pension because of this, the priority here was to advise him about what was best for his retirement provisions. Mr E was only 55. An obvious drawback with a personal plan's death benefits is that the amount left to pass on – to anyone – may be substantially reduced as the pensioner starts to withdraw his or her retirement income. To this end, if Mr E had lived a long life there could be nothing left at all in his personal pension plan. It also doesn't appear that Makemson took into account the fact that Mr E could have nominated a beneficiary of any funds remaining in his other (TATA) DC scheme. So, to this end, Mr E already had options ensuring part of his pension wouldn't 'die with him'.

- It's clear that Mr E, like many employees of his company, was concerned about his pension. However, I think that Makemson should have reassured Mr E that the scheme moving to the PPF wasn't as concerning as he thought. The income available to Mr E through the PPF would have still probably provided a significant portion of the income he would have needed at retirement, and he was still unlikely to be able to exceed this by transferring out, given his real ATR and the effect of pension charges and fees. And although the increases in payment in the PPF were lower than the BSPS, the income was still guaranteed and was not subject to any investment risk. So, I don't think that these concerns should have led to Makemson's recommendation to Mr E to transfer out of the DB scheme altogether.

Summary

I don't think the advice given to Mr E was suitable.

He was giving up a guaranteed, risk-free and increasing income within the PPF. By transferring to a personal pension, the evidence shows Mr E was likely to obtain lower retirement benefits. And I don't think there were any other particular reasons which would justify the transfer and outweigh this. I think Makemson ought to have advised him against transferring out of his DB scheme for this reason, particularly as it meant he'd possibly be worse off in retirement.

So, I don't think it was in Mr E's best interests for him to transfer his DB scheme to a personal pension when he had the opportunity of opting into the PPF. On this basis, I think Makemson should have advised Mr E to allow his DB benefits to move to the PPF.

In light of the above, I think Makemson should compensate Mr E 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 Makemson to put Mr E, as far as possible, into the position he would now be in but for Makemson's unsuitable advice. I consider Mr E would have most likely moved his pension to the PPF, rather than transfer to the personal pension if he'd been given suitable advice and compensation should be based on his normal retirement age of 65, as per the usual assumptions in the FCA's guidance. Makemson should use the benefits offered by PPF for comparison purposes.

Makemson has sought to argue an earlier retirement age should be used in the eventual calculation and has cited what Mr E did eventually go on to do, that is, to draw some of his transferred benefits early. But this uses the benefit of hindsight as Mr E has since decided to draw some pension benefits only because of the situation he finds himself in, after receiving the unsuitable advice to transfer. He also started drawing the benefits later than the age of 57. When deciding on using the NRA 65 as the retirement age, I've considered DISP Application 4.3.15 - 4.3.17 in particular.

Makemson must therefore undertake a redress calculation in line with the rules for calculating redress for non-compliant pension transfer advice, as detailed in policy statement PS22/13 and set out in the regulator's handbook in DISP App 4:
https://www.handbook.fca.org.uk/handbook/DISP/App/4/?view=chapter.

Makemson should use the FCA's BSPS-specific redress calculator to calculate the redress. And Mr E needs to now promptly provide Makemson with his current pension details and balance so this can be done. A copy of the BSPS calculator output should be sent to Mr E and the Financial Ombudsman Service upon completion of the calculation.

This calculation should be carried out using the most recent financial assumptions in line with DISP App 4. In accordance with the regulator's expectations, this should be undertaken or submitted to an appropriate provider promptly following receipt of notification of Mr E's acceptance of my final decision.

If the redress calculation demonstrates a loss, as explained in policy statement PS22/13 and set out in DISP App 4, Makemson should:

- calculate and offer Mr E redress as a cash lump sum payment,
- explain to Mr E before starting the redress calculation that:
    - the redress will be calculated on the basis that it will be invested prudently (in line with the cautious investment return assumption used in the calculation), and
    - a straightforward way to invest the redress prudently is to use it to augment their DC pension
- offer to calculate how much of any redress Mr E receives could be augmented rather than receiving it all as a cash lump sum,
- if Mr E accepts Makemson's offer to calculate how much of the redress could be augmented, request the necessary information and not charge Mr E for the calculation, even if he ultimately decides not to have any of the redress augmented, and
- take a prudent approach when calculating how much redress could be augmented, given the inherent uncertainty around Mr E's end of year tax position.

Redress paid to Mr E as a cash lump sum will be treated as income for tax purposes. So, in line with DISP App 4, Makemson may make a notional deduction to cash lump sum payments to take account of tax that consumers would otherwise pay on income from their pension. Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to Mr E's likely income tax rate in retirement – presumed to be 20%. So making a notional deduction of 15% overall from the loss adequately reflects this.

Our investigator recommended that Makemson should pay Mr E for the distress and inconvenience caused by the unsuitable advice. I have considered the impact this would likely have had on Mr E in his particular circumstances. This pension at the time represented most of his retirement provision. In his situation I think the thought of losing material benefits would have impacted upon Mr E. So I agree the recommended payment of £300 for distress and inconvenience. Makemson should pay Mr E this amount in addition to the redress I've set out above.

Where I uphold a complaint, I can award fair compensation of up to £160,000. *This is a maximum figure and may not be relevant in this case.*

My final decision

<u>Determination and money award</u>: I am upholding this complaint and I now direct Makemson & Company Limited to pay Mr E the compensation amount as set out in the steps above, up to a *maximum* of £160,000.

If Mr E accepts my final decision, the money award becomes binding on Makemson & Company Limited.

My recommendation would not be binding. Further, it's unlikely that Mr E can accept my decision and go to court to ask for the balance. Mr E 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 E to accept or reject my decision before 7 February 2024.

Michael Campbell
Ombudsman