DRN-3775422

The complaint

Mr B complained that he was given unsuitable advice to transfer his defined benefit (DB) pension scheme, to a type of personal pension plan.

Parker Kelly Financial Services Limited is responsible for answering this complaint and so to keep things consistent, I'll refer mainly to "PKFS".

What happened

Mr B approached PKFS in 2017 to discuss his pension and retirement needs. The parties were known to each other, PKFS having previously provided Mr B with financial advice.

The pension in question was 'deferred' and was related to a previous employment Mr B had with a large company, several years previously. The cash equivalent transfer value (CETV) of the pension was approximately £167,748 and the normal retirement age (NRA) was 65.

PKFS completed a 'fact-find' to gather information about Mr B's circumstances and objectives. It also carried out an assessment of his attitude to risk, which it deemed to be "balanced / average". Information gathered by PKFS about Mr B was broadly as follows:

- Mr B was 64 years old, married with no dependent children.
- Mr B ran a business and earned in the region of £150,000 per year. Mrs B earned around £20,000 from her own business.
- He was described as being in good health at the time of the advice, but he had an ongoing medical condition which required monitoring.
- PKFS said Mr B's home and business together amounted a substantial amount.
- Mr B also had a defined contribution (DC) personal pension of his own. This pension is not the subject of a complaint.

On 13 December 2017, PKFS advised Mr B to transfer his pension benefits into a personal pension plan arrangement. It noted he wanted to buy a holiday home overseas with the tax-free lump sum he'd be able to access by transferring. It also put forward some reasons of 'flexibility' for the transfer, which it said suited Mr B's circumstances. Mr B followed the advice but in 2021 he complained to PKFS because he thought the transfer advice had been unsuitable for him. Mr B is represented in bringing the complaint and said he wasn't given enough information and that he's suffered a loss as a result of PKFS's advice.

He later referred his complaint to our Service. One of our investigators looked into the complaint and said it should be upheld. In response, PKFS said it hadn't done anything wrong and was acting on the financial objectives Mr B had at the time. As the complaint couldn't be resolved informally, it's 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 Business ('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 PKFS'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've also comprehensively considered PKFS's responses to the complaint. 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, PKFS should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr B's best interests.

I've used all the information we have to consider whether transferring away from Mr B's DB scheme, to a personal pension, was in his best interests.

I don't think it was, so I'm upholding Mr B's complaint.

Financial considerations / comparisons

Normally, in pension transfer cases, I'd have expected to see some comparisons about whether transferring out was financially viable. And often I'd expect to see this demonstrated in the 'critical yield' figures which would come from an analysis carried out or commissioned by the adviser.

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. It is therefore part of a range of different things which help show

how likely it is that a personal pension could achieve the necessary investment growth for a transfer-out to become financially viable.

However, in this case PKFS didn't carry out such analysis. This is because Mr B was already 64 years of age and the NRA of his scheme was 65. As he had only a few more months before reaching the NRA, I agree that this type of analysis would have been of very limited value. This means that a relatively straightforward comparison of whether his pension could grow by enough outside the DB scheme to make the transfer worthwhile isn't available, nor is it really relevant here.

Mr B's age and circumstances were somewhat different to those we normally see in these types of complaint. I think it's fair to say, for example, that Mr and Mrs B were relatively well off financially, by the standards of most people. Mr B earned £150,000 per year.

I also accept that Mr B's business interests would have meant that 'retirement' probably meant different things to him. We now know he continued to have an involvement in his business for a period thereafter and his 'high' salary continued beyond the age of 65 meaning he was an *additional rate* taxpayer. He then subsequently reduced his income considerably, but would have still been a *higher rate* taxpayer. Given his circumstances, I think it's likely Mr B would / will remain a higher rate taxpayer. This becomes relevant further down.

However, as a DB scheme, the amount he'd receive in retirement for the question I'm looking into here, was pre-determined and he'd have been able to see what his annual pension would be. As this wasn't a DC scheme, this pension didn't have the flexibility to pay Mr B more in certain years over others.

<u>Early stages / information gathering</u>

PKFS was contracted to give Mr B regulated financial advice. So, I think it's fair to hold the firm to the standards we'd expect to see in gathering information about a client before advising them to irreversibly transfer away from a DB pension scheme. I think PKFS will understand this and also that it needed to be mindful of the 'starting point' as dictated by the regulator- that transferring away from such a scheme should first be considered unsuitable.

I acknowledge PKFS may have had a previous and ongoing relationship with Mr B, but I think there were some shortcomings in the information gathered by PKFS on the relevant forms during this advice. This is important, because PKFS needed to demonstrate clearly why transferring-out was suitable at the time. Like our investigator, I think the details of an apparent holiday home purchase were mentioned - but they were unclear. I can't see evidence this 'plan' was discussed in any great depth, for example, showing what the overall costs of the house were or level of funds required to complete the purchase. And PKFS itself acknowledges that the option of taking a loan out for this ought to have been discussed, rather than only considering the transfer from his DB scheme pension. Mr and Mrs B appeared to have a large disposable income available to them, so I think there were a lot of other potential options that should have been considered if this house purchase really was a reason PKFS was using to add weight to the transfer rationale, rather than him transferring away from this pension.

I also find some of the omissions about Mr B's broader financial assets on the 'fact-find' to lack credibility. He and Mrs B appeared to have property and business assets of £3.4 million, but no savings or non-pension investments were recorded. Under "current employment details", the 'fact-find' also implied Mr B's current intentions were to retire at the age of 65. I think this is either an error, or it raises fundamental questions about the suitability of the recommendations, which I'll explain about below. PKFS also failed to investigate what Mr and Mrs B retirement income needs were likely to be. As he was almost 65 and Mrs B was already 65, I think this was relevant if considering a pension transfer because it was important to consider what income they had to live on. Mr B's other (DC) pension was relatively modest and Mrs B's pension (if she had one) wasn't recorded at all. Both were due to receive the state pension, but none of this was discussed in any detail according to documents I've seen. In short, what Mr and Mrs B would use to fund their retirement wasn't made clear enough.

The recommendation

What we know about the advice is that PKFS recommended Mr B to transfer the £167,748 away from his DB scheme. PKFS said if he made this transfer, he could then access 25% of this tax-free, as per the rules, and invest the remained in his 'other' pension – an existing DC scheme. The advice was essentially based on the following rationale:

- There was a mention that Mr B wanted to use the transferred funds to help buy a home oversees.

- If he didn't transfer from the DB scheme, he could still take some tax-free cash when he reached 65, but the remaining 75% would be subject of 45% tax because Mr B was currently an *additional rate* taxpayer.

- If he transferred away from the DB scheme, the tax-free element he could access would be around £41,000, rather than only around £32,000 if remaining with the DB scheme.

I've therefore considered these issues in turn.

- *The holiday home overseas*

As I've said, I've seen no detailed information about this. I accept it was discussed as it was recorded on documentation from the time. The recommendation report said, *"the funds from the* [tax-free lump sum] *are to be used to fund the purchase of a holiday home."* But there's nothing showing Mr and Mrs B wouldn't have been able to afford this from other sources. Whilst there were no savings or investments recorded in the 'fact-find' what I've seen elsewhere implies differently. We can see, for instance, that a mortgage existed on their main residence and a reason for this was that Mr B preferred to retain "control of capital". I also think their circumstances strongly suggest they would have some other means / capital available to them. Mr B also appears to have removed some tax-free cash from his 'other' DC pension at some point, but the whereabouts of this money wasn't clear.

So, essentially, we don't know much about this property purchase, how much it was, whether it was a priority – and certainly, why it couldn't be funded by alternative means. 2017 was a very low interest rate period, and Mr and Mrs B appeared to have means to have a deposit and to also borrow in the normal way at very low interest rates. If this purchase really was an objective, then PKFS should have been much clearer in obtaining the right information before recommending the transfer.

- *Tax and tax-free cash*

I think this case and the advice surrounding it was largely about tax. For understandable reasons, Mr B probably wanted to use his wealth efficiently and the adviser clearly wanted to help Mr B legitimately pay as least tax as possible.

If Mr B didn't transfer from the DB scheme, PKFS said he could still take some tax-free cash when he reached the age of 65, but it said the remaining 75% would be paid as an annual pension and therefore at that time be subject of 45% tax; this is because Mr B was then an additional *rate* taxpayer. I of course recognise that whilst a part-owner of the business, this would have meant Mr B would likely continue to be a significant taxpayer for the immediate future. However, I think it's also fair to say the payment of tax at the 45% rate would reduce at some point. And as I pointed out earlier, the 'fact-find' does say his intended retirement from the current role was 65. In any event, I've seen nothing showing that Mr B expected to pay the additional rate tax rate for the rest of his life, and I think the evidence points to this tax rate reducing at some point. This subsequently happened.

I think it's also important to bear in mind that if taking tax-free cash from the DB scheme upon reaching 65, this DB pension would only be £4,800 per year. So if his earnings reduced as it was fairly likely they would, having the annual pension wouldn't likely push him back up to the much higher taxation band.

So I think these things show that using the rationale of Mr B being an additional rate taxpayer didn't necessarily justify the advice to irrevocably transfer away from the DB scheme. His DB pension in payment was relatively low and the likelihood was that Mr B's tax rate would reduce at some point soon. Recommending that he transfer out due to high tax rates wasn't therefore justified.

PKFS also promoted to Mr B that he could access more tax-free cash if he transferred to a personal pension arrangement. It said he'd be able to access 25% of his pension as a lump-sum and then use the remaining funds more flexibly if he transferred away. On the other hand, if sticking with the DB pension and taking a tax-free lump-sum, this would only yield 19% in tax-free cash.

It's usually the case that more tax-free cash can be accessed from a personal pension when compared against a DB scheme; this is because the values and benefits of the two schemes are calculated differently. But PKFS should have been telling Mr B at the time that extra tax-free lump sums being removed from a personal pension also came with consequences in that the amount left for his later retirement years would obviously decrease. In any event, I don't think this difference changes anything. I've already explained how I don't think the holiday home purchase was genuinely material to this advice – and Mr and Mrs B clearly enjoyed wealth from other sources. So, in the unlikely event this immediate difference of £10,000 between the two tax-free lump sums really was crucial, I'd have expected to see this substantially explained in the recommendation. It wasn't and so I think it's reasonable to conclude that it didn't materially matter in his case.

What Mr B was giving up

This is a relatively unusual case in the sense that everything we can see is strongly suggestive of Mr and Mrs B enjoying significant wealth; all the indications are they would probably have a good retirement from a financial perspective.

I think it was fair that PKFS didn't produce critical yield rates, but it failed to set out what Mr and Mrs B's retirement income requirements were and more importantly, how they would meet them. As I've said, I find it unlikely Mr and Mrs B had little or no other savings, but I also accept we simply don't know. In essence, Mr B's pensions were relatively modest affairs: his DC pension had reduced down to around £112,000 after he'd taken some tax-free cash; and (this) DB pension was estimated at either £6,270 (with no lump sum) or £4,800 (with a £32,000 lump sum). These, together with two state pensions, would clearly feel like a significant income reduction to Mr and Mrs B in their particular circumstances, if he did retire soon. And if the DB pension was transferred out completely, I can't see what their plan would have been.

Giving regulated pension transfer advice would have been the obvious point at which to comprehensively set this out. But PKFS didn't do this and so the only rationale that really stands up for transferring is for potentially reducing Mr B's annual income tax burden in the short-term.

The pension also came with a number of benefits and guarantees commensurate with a DB scheme. Mrs B's own pension arrangements were uncertain and so the death benefits in his DB scheme would have been of use to her if Mr B pre-deceased her. It comprised 60% of the full pension. There were also index-linking guarantees (with certain limitations).

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 were probably made to look like attractive features to Mr B. But whilst I appreciate death benefits are important to consumers, and Mr B might have thought it was a good idea to transfer to a personal pension because of this, the priority here was to advise him about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement.

I've noted that PKFS puts forward the notion now that because Mrs B was the older of the two, having the spouse benefits wasn't that important in her case. However, this is a very weak challenge in my view; Mrs B was only marginally older and PKFS puts forward no analysis or credible reasoning for suggesting the spouse's benefits were of little use to her. Under the DB scheme the death benefits were guaranteed and they escalated – they were not dependent on investment performance, whereas the sum remaining on death in a personal pension was. In any event, there may not have been a large sum left anyway in a personal pension upon Mr B's passing, particularly if he lived a long life. PKFS should therefore not have encouraged Mr B to prioritise the potential for higher death benefits through a personal pension over his security in retirement.

It also doesn't appear that PKFS took into account the fact that Mr B could have nominated someone as the beneficiary of any funds remaining in his DC scheme. So, to this end, Mr B had already ensured part of his pension wouldn't 'die with him'.

Summary

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

Ultimately, I don't think the advice given to Mr B was suitable. He was giving up a guaranteed, risk-free and increasing income within the DB scheme. By transferring to a personal pension arrangement, the evidence shows Mr B 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 PKFS ought to have advised him against transferring out of his DB scheme for this reason, particularly as the analysis was so poor about what he'd live on in retirement.

So, I don't think it was in Mr B's best interests for him to transfer his DB scheme to a personal pension when he had the opportunity of remaining where he was. On this basis, I think PKFS should have advised Mr B to continue with his DB scheme and access it as the scheme was originally intended.

I have considered, given the circumstances of the time, whether Mr B would have transferred to a personal pension in any event. I accept that PKFS disclosed some of the risks of transferring to Mr B, and provided him with a certain amount of information. But ultimately it advised Mr B to transfer out, and I think Mr B relied on that advice.

I'm not persuaded that Mr B would have insisted on transferring out of the DB scheme, against PKFS's advice. I say this because this pension accounted for a reasonable proportion of his retirement provision at the time. So, if PKFS 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 have accepted that advice.

In light of the above, I think PKFS should compensate Mr B 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 B, as far as possible, into the position he would now be in but for PKFS's unsuitable advice. I consider Mr B would have most likely remain in his DB scheme, rather than transfer to the personal pension if he'd been given suitable advice. So, PKFS should use the benefits offered by his DB scheme for comparison purposes.

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 B whether he preferred any redress to be calculated now, in line with current guidance, or wait for any new guidance/rules to be published. He didn't specify, so I am satisfied, as we've originally said, that a calculation in line with FG17/9 remains appropriate and, if a loss is identified, will provide fair redress for Mr B.

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 B's acceptance of the decision.

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

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Mr B'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 B 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 40%. So making a notional deduction of 30% 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 B within 90 days of the date PKFS 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 PKFS to pay Mr B.

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 PKFS 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 £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've decided to uphold this complaint.

I now direct Parker Kelly Financial Services Limited to pay Mr B 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 Parker Kelly Financial Services Limited to pay Mr B any interest on that amount in full, as set out above. Where the compensation amount already exceeds £160,000, I would only require Parker Kelly Financial Services Limited to pay Mr B any interest as set out above on the sum of £160,000.

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

If Mr B accepts my final decision, the money award becomes binding on Parker Kelly Financial Services Limited.

My recommendation would not be binding. Further, it's unlikely that Mr B can accept my decision and go to court to ask for the balance. Mr B 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 B to accept or reject my decision before 21 March 2023.

Michael Campbell
Ombudsman