DRN-3835170

The complaint

Mr H complains about the suitability of the advice provided by Inspirational Financial Management Ltd ("IFM") in September 2017 to transfer the value of his safeguarded benefits in the British Steel Pension Scheme ("BSPS") to a personal pension plan ("PPP").

What happened

In March 2016, Mr H's employer, Tata Steel UK Ltd ("Tata Steel"), announced that it would be examining options to restructure its business including decoupling the BSPS from the company. The BSPS was a defined benefits ("DB") pension scheme that provided a guaranteed lifetime income to members. The consultation with members referred to possible outcomes regarding their safeguarded benefits, one of which was a transfer to the Pension Protection Fund ("PPF") – the PPF is a statutory fund designed to provide compensation to members of DB pension schemes when their employer becomes insolvent.

In March 2017, Tata Steel closed the BSPS to further benefit accrual. By that point, Mr H had accrued 28 years and 4 months' qualifying service in the BSPS between January 1988 and May 2016. His annual scheme pension as at the date of leaving the scheme in May 2016 was £13,231.10.

In May 2017, the PPF announced that the terms of a Regulated Apportionment Arrangement ("RAA") had been agreed – this was approved by The Pensions Regulator in August 2017. Under the announced plans, Tata Steel agreed to set up and sponsor a new DB pension scheme, the BSPS2, subject to certain conditions relating to funding and size being satisfied.

Mr H was concerned about what the announced changes meant for the security of his safeguarded benefits in the BSPS and wanted advice on his options. The cash equivalent transfer value of his safeguarded benefits at that time was £332,207.40. In August 2017 he contacted another business ("Firm A") to get advice. Since Firm A didn't have the necessary regulatory permissions to advise on pension transfers, it introduced Mr H to IFM. One of IFM's advisers recorded the following information about Mr H:

- He was aged 47, divorced and in good health. He didn't have any children or other people financially dependent on him;

- He was employed full-time by Tata Steel and paid gross annual income of about £33,000;

- His assets comprised his home which was encumbered with a mortgage. The value of his home and any savings or investments he had wasn't recorded;

- Other than the mortgage on his main residence (the outstanding loan value wasn't recorded), he didn't have any other debts or liabilities;

- After paying for bills and essentials, he had surplus disposable income of about £300 to £600 available every month;

- In addition to the value of his safeguarded benefits in the BSPS, he was on course to receive the full state pension at age 67 and had been a member of Tata Steel's defined contribution ("DC") pension scheme since June 2016. The total annual contribution into his DC plan was 12% of his gross annual salary (the value of his DC plan wasn't recorded but, by that point, total contributions of about £4,000 had been invested);

- He was an inexperienced investor. On a scale of 1 to 5 where 1 (Cautious risk) was lowest risk and 5 (Adventurous risk) was highest risk, his risk profile was determined to be 1 or *'Cautious risk'.* This was defined as, *"I am a cautious investor who requires little risk to their pension capital. I seek stability and conservative growth. I consider security to be generally more important than increasing my income.";* and

- His primary objective regarding his safeguarded benefits was to retire earlier than the BSPS normal retirement age of 65. He wanted to retire from age 55 or as soon as possible after that age.

Following the fact find meeting, IFM's adviser issued his suitability report in September 2017. This explained to Mr H that he had three options regarding his safeguarded benefits:

1. Transfer to the PPF;
2. Transfer to the BSPS2; or
3. Transfer to an alternative pension plan such as a PPP.

IFM's adviser recommended that Mr H transfer to a PPP provided by Prudential for the following reasons:

- *"You require the flexibility to control and tailor the frequency and amount of income you receive from your pension fund in retirement to suit your circumstances, needs and tax position, as opposed to the pre-set (albeit guaranteed) income that your existing defined benefits pension would provide.*

- *You want to ensure you can retire when you want and do not want to take the risk of having restrictions in place when the scheme enters the PPF or it becomes the 'new' British Steel Pension Scheme.*

- *You are prepared to accept more risk in return for greater flexibility over when and how benefits are withdrawn from your pension fund."*

The costs associated with the recommendation were as follows:

Initial advice charge

- 1.44% (or £4,800) – initial adviser charge for recommendation and implementation

Ongoing annual charges

- 0.65% investment annual management charge deducted from the PPP fund value

- 0.35% product fee deducted from the PPP fund value

- The basis of the recommendation was that following the pension transfer, Firm A, who introduced Mr H to IFM, would provide ongoing advice regarding the management and investment of the recommended PPP. In connection with this, IFM's adviser stated in the suitability report, *"It is important that your funds and financial planning arrangements are reviewed at regular intervals to ensure that they remain suitable. I understand this service will be provided by* [Firm A]*. The cost of this provision can be paid directly by you or can be taken from your pension fund on an ongoing basis. This is something you and* [Firm A] *will need to discuss and agree on."* The cost of that ongoing advice wasn't stated in the suitability report.

IFM calculated Mr H's estimated revalued annual scheme pension at age 65 as £20,842.10 on the basis he took a full scheme pension only. It calculated the critical yield to match that benefit as 6.7%. The calculation assumed 0% ongoing advice costs. The critical yield at age 55 – to align with the age at which Mr H wanted to retire – wasn't calculated.

Mr H accepted the recommendation, following which the transfer to the PPP was completed. IFM recommended that the PPP fund value be invested in the following fund to align with Mr H's '*Cautious risk*' profile:

Fund	**Allocation**	**Estimated annual growth rate before charges**
Prufund Cautious	100%	5.50%

<u>This complaint</u>

During 2022, Mr H complained to IFM about the suitability of its pension transfer advice. He thought that the advice had caused him to suffer a financial loss.

IFM didn't uphold this complaint. In summary, it stated that Mr H was concerned about the issues surrounding Tata Steel and the security of his safeguarded benefits in the BSPS. It considered that the continuing uncertainty at the time was sufficient reason for Mr H to transfer away so that he could obtain control of his safeguarded benefits and benefit from the flexibility to withdraw variable amounts of money from age 55 and leave a lump sum to his beneficiaries on death. It was satisfied that it had adhered to and considered relevant FCA rules and guidance including providing Mr H with all the necessary information and risk warnings in good time to be able to make an informed decision. In its view, the pension transfer to the PPP was in his best interests and so was therefore suitable.

One of our investigators considered this complaint and recommended that it be upheld because, in his view, IFM failed to demonstrate that transferring to the PPP was clearly in Mr H's best interests at the time. He thought suitable advice would've been to transfer to the BSPS2. To put things right, our investigator recommended that IFM carry out a redress calculation in line with the FCA's guidelines on the basis that Mr H transferred to the BSPS2, took benefits at age 65 and would be a 20% income taxpayer in retirement. In addition, he recommended that IFM pay Mr H £300 compensation for the trouble and upset caused by its unsuitable recommendation.

Mr H accepted our investigator's assessment. Despite several chasers, IFM didn't provide its response to our investigator. Since agreement couldn't be reached, this complaint has been referred to me to review and decide. This is the last stage of our process.

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. 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.

Mr H's situation

The situation for Mr H wasn't normal because the existing DB pension scheme, the BSPS, was closing. So he was essentially forced to transfer the value of his safeguarded benefits to a new scheme. He had three options:

1. Transfer to the PPF;
2. Transfer to the BSPS2; or
3. Transfer to an alternative pension plan such as a PPP.

It's undeniable that it was a period of great uncertainty for individuals such as Mr H. Many of these individuals were in a vulnerable position due to the uncertainty surrounding the future of the BSPS. I think the uncertainty only served to emphasise the need at that time for a balanced assessment of the options available and ultimately the provision of suitable advice.

Options 1 and 2 would've enabled Mr H to retain guaranteed lifetime income, albeit at a lower level than provided by the BSPS. So while the situation was somewhat unusual, Mr H still had the option to retain guaranteed benefits in either the PPF or BSPS2. IFM stated in its suitability report that full details of the BSPS2 weren't known at that stage but were expected to be announced shortly.

I don't believe that the circumstances surrounding the BSPS altered the FCA's position or its expectations of firms. Given the FCA's view on safeguarded benefits and what was known at that time, it's my fair and reasonable opinion that IFM should've delayed its advice until more information about the BSPS2 became available. And once those details became available to only recommend a transfer to the PPP in favour of the BSPS2 if it could *clearly* demonstrate it was in Mr H's best interests, as referenced in COBS 19.1.6G.

Despite several chasers, IFM didn't provide its response to our investigator's assessment. I'm satisfied that I've been provided with sufficient evidence to decide this complaint. Having considered the evidence, I agree with the investigator's view that IFM's pension transfer advice to Mr H was unsuitable for largely the same reasons. In summary:

- Mr H's safeguarded benefits, accounting for 28 years and 4 months' qualifying service, represented the backbone of his retirement provision built up by that time. So I think it's fair to say that when he came to retire he would be heavily reliant on the value of his safeguarded benefits to generate a minimum level of core income to support his standard of living in retirement. IFM recorded that he was an inexperienced investor with a *'Cautious risk'* profile which was defined as, *"I am a cautious investor who requires little risk to their pension capital. I seek stability and conservative growth. I consider security to be generally more important than increasing my income".* Transferring to the PPP led to the investment, inflation and longevity risk being transferred from the scheme to Mr B. Taking these factors into account, it's my view that there needed to be a compelling reason why it was suitable for Mr H to transfer to the PPP compared to the alternative option of retaining guaranteed lifetime income under the BSPS2;

- Mr H was then aged 47. IFM recorded that he wanted to retire from age 55 or as soon as possible after that age. With such a time horizon until pension benefits could be accessed, it makes the case for a pension transfer – for the sake of achieving possible early retirement – more difficult to justify. Had IFM advised Mr B to transfer to the BSPS2 he would've maintained safeguarded benefits and retained the option to transfer to a PPP at a later date, if then deemed suitable, when he could immediately access benefits and, crucially, determine his retirement income and lump sum needs with far greater accuracy than at age 47;

- IFM stated that Mr H was *"prepared to accept more risk in return for greater flexibility over when and how benefits are withdrawn from your pension fund".* I'm not persuaded that it was appropriate for an inexperienced and *'Cautious risk'* investor like Mr H to relinquish the guarantees attached to his main retirement provision in exchange for more risk so that he could access flexible benefits. Flexibility and control might sound attractive, but I can't see that Mr H had any concrete need for it. It was recorded that he preferred *"choice and control"* over guaranteed lifetime income, however I'm not sure what this was based on. He had received guaranteed income all his working life and a *'Cautious risk'* profile. So I think a guaranteed income would've been valuable for an individual in Mr H's circumstances. In any event, he was expected to continue contributing 12% of his annual salary into his workplace DC plan for at least the next several years. So he would've had flexible options available through the TFC available under the BSPS2 and the DC plan without taking risk on his main pension provision;

- I think the suitability report misled Mr H about the ability to take early retirement benefits under the PPF and BSPS2 options. It stated, *"Early retirement is unlikely to be an option under the PPF…whilst the terms and conditions of the British Steel 2 Pension Scheme are not fully known".* The reference to the PPF is incorrect since members are entitled to take benefits early from age 55 onwards subject to a reduction. The same was also true for the BSPS2. IFM portrayed the reduction as a penalty. But it wasn't a penalty. Rather, the reduction was applied to reflect the fact that the BSPS2 would have to support the income for longer than anticipated, and to protect the interests of scheme members generally. And so, based on what IFM said, it's likely Mr H incorrectly believed he would be unfairly treated if he took benefits early under the BSPS2 when this wasn't actually the case;

- IFM portrayed the PPP option as allowing for early retirement earlier than age 65 without penalty. I think this was misleading. The reality was of course that the PPP would've had less time to grow if accessed earlier than age 65 and any resulting income would need to last longer. I cannot see that this was adequately explained to Mr H so that he could understand accessing any of the available options early would likely lead to reduced retirement income during his lifetime compared to taking benefits at age 65. So I think he made the decision to transfer from an uninformed position in this regard;

- IFM calculated the critical yield to match the benefits under the BSPS at age 65 as 6.7%. This compared with a discount rate of 4.4%, as explained by our investigator. I think the critical yield figure of 6.7% was misleading and understated the true, higher critical yield. I'll explain why. The basis of the advice was that Firm A would provide ongoing advice to Mr H at a cost – but the cost wasn't stated in the suitability report or taken into account when calculating the critical yield. Including the cost of ongoing advice would've increased the critical yield figure and therefore the growth rate required to match the guaranteed income. And so I think IFM misled Mr H in this regard;

- Notwithstanding this, the basis of the recommendation was that Mr H was seeking to take benefits at age 55. If that was the case then I would've expected IFM to also calculate the critical yield figure at that age to enable Mr H to make an informed decision. But it inexplicably only calculated and presented the figure at age 65. I think this is a material oversight because the figure at younger ages would've been higher (compared to at age 65) due to the shorter investment timeframe and impact of the initial advice charge on the required growth rate. This means that Mr H wasn't provided accurate information about the level of investment growth required to match the scheme pension if he took benefits early. And so the critical yield figure at age 55 was likely to be well in excess of 6.7%. It's my view that such a rate of required investment growth was incompatible with Mr H's *'Cautious risk*' profile, discount rate and the estimated annual growth rate of 5.50% (before charges) of the recommended investment strategy. I think it was clear that Mr H would be worse off as a result of the pension transfer;

- IFM recorded that Mr H was divorced and didn't have any children or other people financially dependent on him. But a change in the format of death benefits was mentioned by IFM as another reason for transferring to the PPP to provide benefits for unspecified beneficiaries. While I understand that death benefits are important to consumers, the priority here, in my opinion, was to advise Mr H about what was best for his own retirement provision. A pension is primarily designed to provide income in retirement. It's my view that Mr H had no health issues at the time IFM advised him which might reasonably have prompted him to relinquish the guarantees attached to his own retirement income for the sake of providing benefits to unspecified beneficiaries;

- IFM portrayed the PPF as an option to avoid because it would *"restrict"* Mr H's retirement. I think this was an unfair representation of the PPF. While I understand Mr H was concerned about the security of his safeguarded benefits, I don't consider a transfer to the PPF was an outcome for him to avoid. Under the PPF Mr H would've received a minimum of 90% of his scheme pension. This contrasted with the recommended PPP where there's no promise of a minimum level of benefits payable. If Mr H was concerned about his safeguarded benefits being transferred to the PPF which would result in him losing 10% of his scheme pension, then I question why, as a *'Cautious risk'* investor, he would accept the risk of transferring to a PPP which exposed him to unlimited downside risks where the loss could be significantly greater than 10%. This doesn't make sense to me; and

- Overall, I don't think the contemporaneous evidence supports the position as to why flexibility and early retirement objectives would've been sufficiently compelling reasons for Mr H to relinquish valuable benefit guarantees at that time by transferring to a PPP. I haven't seen any evidence that persuades me the pension transfer to the PPP led to Mr H gaining any clearly defined advantage compared to the alternative option of transferring to the BSPS2. As a result, I think it's fair and reasonable to uphold this complaint.

Putting things right

A fair and reasonable outcome would be for IFM to put Mr H, as far as possible, into the position he would now be in but for the unsuitable advice he was given. My view is aligned with that of our investigator.

Our investigator concluded that, if properly advised, Mr H would've transferred to the BSPS2 and his benefits would now be preserved in that scheme. While some information on the benefits of the BSPS2 were still to be confirmed, it's my view that by September 2017 the risk of the BSPS falling into the PPF had receded by a large extent following the announcement by the PPF in May 2017 that the terms of a RAA had been agreed. So I think

IFM should've considered the BSPS2 as a viable option. So, in addition to the PPF, I think it's fair to consider the BSPS2 as a potential comparator scheme for redress purposes.

There were differences between the BSPS2 and PPF. These differences meant that the PPF was likely the better option for unmarried, deferred members who expected to retire early or take the maximum tax-free cash available even allowing for the 10% reduction in the starting entitlement. But the BSPS2 was likely the better option for married pensioners and deferred members who expected to draw benefits at or close to the scheme normal retirement age of 65. I'm not convinced that it could be reasonably determined in 2017 that the PPF was the likely better option for Mr H. And so I think, given the lack of clarity surrounding when Mr H would retire, the BSPS2 was likely the better option for him based on what was known at the time and that at age 65 the BSPS2 would provide a higher level of benefits than the PPF. As such, the calculation on the basis of entering the BSPS2 should be carried out. For clarity, compensation should be based on the BSPS2's normal retirement age of 65, as per the usual assumptions in the FCA's guidance.

IFM 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.

The 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 H's acceptance of this final decision.

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

- calculate and offer Mr H redress as a cash lump sum payment,
- explain to Mr H before starting the redress calculation that:
  - its 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 his PPP
- offer to calculate how much of any redress Mr H receives could be augmented rather than receiving it all as a cash lump sum;
- if Mr H accepts IFM's offer to calculate how much of his redress could be augmented, request the necessary information and not charge Mr H for the calculation, even if he ultimately decides not to have any of his redress augmented; and
- take a prudent approach when calculating how much redress could be augmented, given the inherent uncertainty around Mr H's end of year tax position.

Redress paid to Mr H as a cash lump sum will be treated as income for tax purposes. So, in line with DISP App 4, IFM 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've been taken as tax-free cash and 75% would've been taxed according to Mr H'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.

In addition, IFM should pay Mr H £300 compensation for the trouble and upset caused by its unsuitable recommendation, as recommended by our investigator.

My final decision

Determination and money award: I uphold this complaint and require Inspirational Financial Management 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 doesn't exceed £160,000, I would additionally require Inspirational Financial Management 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 Inspirational Financial Management 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 Inspirational Financial Management 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 final decision, the money award becomes binding on Inspirational Financial Management Ltd. My recommendation wouldn't be binding. Further, it's unlikely that Mr H can accept this final 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 this final decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 7 November 2023.
Clint Penfold
Ombudsman