DRN-3966521

The complaint

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

Mr H is represented in this complaint, but for ease I'll refer only to Mr H.

What happened

Mr H and his wife Mrs H approached KMD in December 2016 to discuss their pensions and retirement needs. Mr H later told our Service this was because they were worried about Mr H getting another job at that time, so they thought they might access Mrs H's pension benefits to tide them over until Mr H reached age 60 and could access his own pension benefits. Mr H says KMD then began looking at his pension too.

KMD gathered information about Mr H's circumstances and objectives. Mr H was age 52 and was married with three children, one of whom was a dependent. Mr and Mrs H were both employed with net annual employment income of £14,000 for Mr H and £25,500 for Mrs H, with Mr H having additional annual rental income of £5,500. Their joint annual expenditure was £42,000, though KMD didn't record any detail about how that amount was reached.

Mr H and Mrs H owned three properties worth about £500,000 in total – they had two repayment mortgages for these, with outstanding balances totalling £107,000 for which they paid £750 in total each month with 16 years left on the mortgage terms. Mr H and Mrs H had no other debt. They had joint savings of £2,000 and shares from an employer valued at £13,000 (Mr H) and £10,000 (Mrs H). Mr H had decreasing term life insurance with a sum assured of £106,807, and expected to receive an inheritance of about £50,000 in the future. Mr H also had three pensions – a DB pension with a cash equivalent transfer value ('CETV') of £1,115,936.53 plus a linked additional voluntary contribution plan worth £10,136.84, and a defined contribution ('DC') occupational pension that had just started. Mrs H had two pensions – one with a transfer value of about £150,000 and a DB occupational pension with a pot of about £17,000.

KMD also carried out an assessment of Mr H's attitude to risk, which it deemed to be 'high medium', or six out of ten.

In February 2017, KMD advised Mr H to transfer his main DB pension into a personal pension. It said this would allow Mr H to achieve his objectives of having control and flexibility over his retirement income, including the option to withdraw tax free cash ('TFC') only, and to have better death benefits for his wife and family. Mr H accepted this advice, so £1,115,936.53 was transferred from his DB scheme to a new personal pension.

In 2019, Mr H accessed £100,000 of TFC when he reached age 55. He says he used this TFC to repay a mortgage held by him and his wife, and a mortgage held by his son.

In 2021, Mr H complained to KMD that its 2017 advice to transfer had been unsuitable because he'd lost guaranteed benefits from his DB scheme, KMD had assessed his attitude to risk too highly, and hadn't properly explained his future lifetime allowance ('LTA') tax liabilities.

KMD didn't uphold Mr H's complaint. It said the transfer met Mr H's objectives and that he was always going to transfer, as he'd already obtained his DB pension's CETV prior to approaching KMD. And KMD said it had carried out a thorough process in line with the regulator's requirements, had fully considered Mr H's circumstances and options, correctly assessed his attitude to risk and capacity for loss, and explained the risks and benefits to him. So Mr H had made an informed decision to accept to transfer.

Mr H referred his complaint to our Service. One of our Investigator's upheld it. She thought KMD's 2017 advice to transfer the DB pension was unsuitable because it would leave Mr H worse off in retirement and there were no compelling reasons to transfer. She said KMD should put Mr H into the position he'd have been in but for its unsuitable advice in 2017 and carry out a redress calculation on that basis.

Mr H agreed with our Investigator's view.

But KMD disagreed with our Investigator. It reiterated Mr H would've transferred anyway, because he'd already contacted another financial adviser and obtained a CETV before speaking to KMD, and he'd told KMD he wanted a guarantee he and his wife could transfer their DB pension benefits into personal pensions. KMD said it hadn't encouraged Mr H to look at his transfer options and told him not to transfer if he wanted guaranteed income or had any doubts. It said Mr H was informed, well-educated and worked at a senior level, and was keen to have control over his pension. And he still wanted to transfer his DB benefits, so KMD recommended he transfer them. KMD argued Mr H wanted TFC as early as possible, which he accessed. That his savings, investments, and properties meant he had significant capacity for loss. And that Mr H might retire at age 60 but might also work past this, and his new personal pension gave him this flexibility.

Our Investigator wasn't persuaded to change her opinion, and so the complaint was referred for an Ombudsman to make a final decision.

Whilst that referral was underway, our Service contacted both Mr H and KMD to explain that Mr H could choose to have any redress calculated now in line with the regulator's current guidance in FG 17/9, or he could instead choose to wait for any new guidance/rules to be published by the regulator, as expected in early 2023.

Mr H confirmed he wanted any redress calculated now in line with the regulator's current guidance, but had nothing else to add. KMD didn't provide a response to this.

On 26 January 2023 I issued my provisional decision. In summary, I said the advice given to Mr H was unsuitable. 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 particular reasons which would justify a transfer and outweigh this. He was also likely to be subject to an LTA tax charge by transferring out. Mr H shouldn't have been advised to transfer out of his DB scheme just to have flexibility and control he didn't need, and the potential for higher death benefits wasn't worth giving up the guarantees associated with his DB scheme. It also wasn't worth the risk of him incurring an LTA tax charge. So, KMD should've advised Mr H to remain in his DB scheme.

In my provisional decision, I said KMD should compensate Mr H for the unsuitable advice, using the regulator's DB pension transfer redress methodology. And I said it should also compensate him for the LTA charge he'd likely incur in future, since this wouldn't be included in the usual DB transfer redress guidance, and I set out the assumptions I thought it was fair and reasonable for KMD to use when calculating this. But that, alternatively, if both parties preferred, KMD could give Mr H an undertaking to pay any LTA charges he incurs in the future (not taking into account further contributions or new pension arrangements).

Mr H didn't provide any further comments or evidence for me to consider, and he didn't express a preference regarding settling his future LTA liability. But he pointed out that KMD was now in the process of being wound up.

KMD provided me with further comments. In summary, KMD said it was no longer trading but professional indemnity cover was in place. KMD reiterated why it thought Mr H would have still transferred anyway. And said it hadn't recommended or encouraged a transfer – a recommendation was not a mandatory part of the advice process at that time. Instead, KMD gave Mr H detailed options and told him that if he wanted guaranteed income or had any doubts, he shouldn't transfer. KMD said it asked Mr H which option he wanted to choose, and he made an informed choice to transfer. KMD had no record of Mr H being worried about job security during the advice. And Mr H's clear objective was full flexibility of his pension, including TFC as required and tax efficient income later. KMD said its full pension modelling was a like for like comparison to assess the sustainability of Mr H's personal pension. And it preferred to calculate and settle the LTA charge at the final decision date.

As both parties have responded to my provisional decision, I'm in a position to make my final decision about Mr H's complaint.

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 must first acknowledge that KMD has stopped trading. KMD has confirmed there is professional indemnity cover in place. But if this doesn't cover Mr H's redress, then Mr H may wish to contact the Financial Services Compensation Scheme ('FSCS'). The FSCS is a scheme of last resort that helps consumers when a financial business is unable – or likely to be unable – to pay compensation due from a claim against the business. Regardless, I don't think anything I've been told about KMD's trading status means I can't make a decision regarding Mr H's complaint against KMD.

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 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 KMD'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 appreciate KMD says it complied with the regulator's requirements. But having considered all of this and the evidence in this case, I'm upholding this complaint.

KMD argues it didn't recommend or encourage a transfer here, but instead gave Mr H detailed options and told him he shouldn't transfer if he wanted guaranteed income or had any doubts, and Mr H made an informed choice to transfer. I see KMD's suitability report noted Mr H liked the flexibility and death benefits available through a personal pension, and included warnings about transferring. But it nonetheless clearly went on to say *"I recommend that you transfer to an Old Mutual Wealth "Collective Retirement Account".* So, I think KMD did recommend that Mr H transfer his DB scheme benefits to a personal pension, and the weight of that recommendation to transfer out can't be ignored.

It may be that KMD is suggesting it simply recommended which personal pension Mr H should invest his DB scheme benefits in, after Mr H had himself chosen to transfer them out. But KMD wasn't there to just transact what Mr H might have thought he wanted. The adviser's role was to really understand what M H needed and recommend what was in his best interests. The regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.6G that the starting assumption for a transfer from a DB scheme is that it is unsuitable. So, KMD 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

KMD carried out a transfer value analysis report (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).

The advice was given during the period when the Financial Ombudsman Service was publishing 'discount rates' on our website for use in loss assessments where a complaint about a past pension transfer was being upheld. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, I consider they provide a useful indication of what growth rates would have been considered reasonably achievable when the advice was given in this case.

Mr H was age 52 at the time of the advice. The fact find recorded that he wanted to retire at age 60, which was his DB scheme's retirement age. KMD now argues Mr H might have gone on to retire much later than this. But nonetheless, KMD's 2017 advice was predicated on Mr H retiring at age 60 - it recorded that the critical yield required to match Mr H's benefits at age 60 was 8.31% if he took a full pension.

This compares with the discount rate of 3.4% per year for seven years to retirement in this case. For further comparison, the regulator's upper projection rate at the time was 8%, the middle projection rate 5%, and the lower projection rate 2%.

I've taken this into account, along with the composition of assets in the discount rate, Mr H's 'high medium' attitude to risk and also the term to retirement. Even if I accepted that KMD had correctly assessed Mr H's attitude to risk, the critical yield was above even the regulator's higher projection rate and so I think 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 that attitude to risk.

The documents provided by KMD include various financial analyses and modelling. KMD may argue that these show Mr H could have been significantly better off in the personal pension plan. I've considered these carefully. They say that under the DB scheme, Mr H was entitled to an annual income of £42,630.87 based on taking a full pension from the scheme at age 60. But KMD recorded that one of Mr H's objectives was to have the option of accessing TFC and taking a reduced pension at age 60, and it argues that this is one of the reasons its advice was suitable for Mr H. But KMD's modelling seems to be based on Mr H accessing a full pension - so it doesn't seem to have taken into account any TFC withdrawal and therefore doesn't reflect what KMD says Mr H wanted to do.

KMD says its full pension modelling was a like for like comparison to assess the sustainability of Mr H's new personal pension. But it's still the case that the modelling doesn't seem to show a direct and meaningful comparison between the escalating income Mr H was entitled to take through his existing DB scheme, and the same income being instead taken through a personal pension to his estimated death. Instead, KMD's modelling shows the various ages at which different levels of annual income from the personal pension will deplete his pension fund. These show the fund would be depleted at some point between age 82 and 98 depending on how much annual income Mr H took and the investment growth rate – so there was a real risk of the funds being depleted before Mr H died. And there may not have been a large sum left, if any at all, to pass on when Mr H died, which I'll return to.

Also, as KMD will know, past performance is no guarantee for future performance and so I consider the discount rates and the regulator's standard projections to be more realistic in this regard in the long term rather than projecting historic returns forward, particularly over such a long period of time.

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 KMD has argued in this case. There might be other considerations which mean a transfer is suitable, despite providing overall lower benefits. I've considered this below.

Flexibility

KMD argues Mr H's clear objective was full flexibility of his pension, including TFC as required and tax efficient income later. But at the time of the advice, I don't think Mr H required flexibility in retirement. In my view, this was more of a 'nice to have' rather than a genuine objective at that particular time. And I don't think KMD properly challenged this with Mr H or made clear to him that while he might wish to access TFC as early as possible and defer taking his retirement income, this was not a pressing need such that he needed to take risks with his DB pension benefits.

I say this because while the suitability report suggests Mr H was attracted to transferring his DB in order to access TFC, it doesn't say anything about why or when he wanted to access TFC, or how much TFC he wanted. I think that if asked, most people might think accessing TFC as soon as possible is desirable. But that doesn't mean it was a genuine objective for Mr H at the time of the advice or one that he should've been encouraged to pursue without good reason. Taking TFC reduces the sum available to provide future retirement income.

Mr H has recently told us that at the time of the 2017 advice, he was worried about getting another job and so they thought they might access Mrs H's pension benefits to tide them over until Mr H reached age 60 and could access his own pension benefits. And he's said this was the reason he and his wife were looking for pension advice, and they approached KMD to see what it would suggest in respect of Mrs H's pension. I should be clear that KMD's documents at the time of the 2017 advice record Mr H as being employed – they don't mention Mr H being concerned about his employment. And KMD has confirmed it has no record of Mr H being worried about his job security at that time. Based on the information provided to me so far, I can see KMD recorded very little about Mr H and Mrs H's objectives at the time of this advice. And what little it did record about Mr H's objectives was general and not in any detail.

If Mr H was in this position, I think KMD could have explored other ways for Mr H to fill a possible income gap for a time if it came to it. Based on what Mr H has more recently told us, it seems he was worried about possibly needing to replace his net annual salary of £14,000 for a time – there's no suggestion that he was worried about his rental income or Mrs H's employment income. So KMD could have considered Mr H and Mrs H's existing savings and shares. It could also have considered the significant capital they had in their three properties – KMD could have introduced the idea of a loan or even selling a property if it became necessary. But in any event this discussion would've been premature. And I think KMD could've advised Mr H to revisit the objective of taking TFC nearer to it becoming available to him at age 55, at which point he'd know how much he wanted and for what reason. He could also then assess whether the TFC available to him through his relatively new DC scheme was sufficient. And I'm mindful that at the time of this advice, Mr H was expecting to receive an inheritance of about £50,000 at some unknown point in the future.

I know Mr H accessed £100,00 of TFC in 2019 when he reached age 55. But as I've explained, at the time of KMD's 2017 advice, I don't think he had any genuine need for TFC such that he needed to take risks with his DB pension benefits. Rather, he was able to take TFC in 2019 simply because KMD's unsuitable advice meant this option was available to him. Mr H has explained he used this TFC towards a mortgage held by him and his wife and a mortgage held by his son, and I've seen nothing to suggest Mr H used this TFC to retire early or fill the potential salary gap he says he was worried about in 2017. Mr H has also explained that he left his last employment in June 2021, and sold a property to allow him to take an extended break from employment with the intention of going back to paid employment in due course.

So overall, I don't think KMD should have advised Mr H to transfer out of his DB scheme to have flexibility and TFC that he didn't really need at that time. Mr H's desire to access his pension doesn't outweigh KMD's responsibility to provide him with suitable advice and act in his best interest. And Mr H would still have retained the option to transfer out of his DB scheme at a later date, should his circumstances dictate that this was in his best interests.

Death benefits

Death benefits are an emotive subject and of course when asked, most people would like their loved ones to be taken care of when they die. The lump sum death benefits on offer through a personal pension 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 KMD explored to what extent

Mr H was prepared to accept a lower retirement income in exchange for the possibility of higher death benefits.

I also think the existing death benefits attached to the DB scheme were underplayed. Mr H was married and had a dependent child and so the spouse's/dependent's pension provided by the DB scheme would've been useful to his spouse and his dependent child if Mr H predeceased them. I don't think KMD 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 the financial modelling provided by KMD shows that Mr H's personal pension fund would be depleted at some point between age 82 and 98 depending on how much annual income Mr H took and the investment growth rate. So there may not have been a large sum left or the fund may have been depleted, particularly if Mr H lived a long life. In any event, KMD 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 wife and children, which didn't depend on investment returns or how much of his pension fund remained on his death, I think KMD should've instead explored life insurance. I appreciate that at the time of the advice, Mr H already had decreasing term life insurance with a sum assured of £106,807. Given the decreasing term and that the sum assured matched Mr H and Mrs H's total outstanding mortgage balance, I think it's likely this life insurance was taken out as protection for the mortgages Mr H held with his wife, and so wouldn't leave Mr H's wife or children with anything once it had been used to repay the mortgages. So KMD should have explored additional life assurance with Mr H if he genuinely wanted to provide more lump sum death benefits for his family.

Based on the documents from the time of the advice, I've seen nothing to suggest Mr H's health meant additional life insurance couldn't have been considered for him, and he and his wife had some disposable income at the time of the advice, albeit Mr H says he was worried about getting another job at that time. But KMD's suitability report doesn't record any discussion about life insurance, and I've not seen that KMD obtained any quotes for life cover for Mr H. So I don't think it gave Mr H enough information on which to base a decision about whether or not this was something he wanted or could afford.

The starting point here should have been for KMD to ask Mr H how much he would ideally like to leave to his wife and any other beneficiaries, and how much he could afford to contribute. Insurance on this basis was likely to be available to Mr H and would have enabled him to leave a legacy without risking his retirement income.

I'm also mindful that Mr H had a newer DC pension he'd be paying into for at least another seven years before his planned retirement age of 60. This fund could've been passed on to a beneficiary of his choice at retirement.

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. And I don't think that the alternative means of providing a legacy for Mr H's wife and children were properly explored.

Control

I think Mr H's desire for control over his pension benefits was overstated. Both Mr H and KMD suggest that Mr H closely followed the movements in value of both his DB pension and his later personal pension. So I accept Mr H had an interest in the value of his funds. But it's still the case that Mr H was not an experienced investor, and I cannot see that he had an interest in or the knowledge to be able to manage his pension funds on his own. This is supported by Mr H choosing to pay KMD 0.3% of the value of his new personal pension each year for ongoing advice. So, I don't think that this was a genuine objective for Mr H – it was simply a consequence of transferring away from his DB scheme.

Lifetime allowance ('LTA')

It appears that because Mr H transferred his DB scheme benefits, he will likely incur an LTA charge in future. This is because when he transferred, the value of the scheme benefits already exceeded the LTA. The benefits from DB schemes are given a value of 20 times the initial annual pension (plus any lump sum that was taken with the pension). According to KMD's transfer value analysis, Mr H's starting pension at age 60 was around £42,630. So, for LTA purposes it would've been ascribed a value of around £852,600. This was below the LTA, so I think that this was another compelling reason not to advise Mr H to transfer his DB scheme.

It appears Mr H raised concerns about this just after KMD delivered its recommendation. However, the adviser reassured Mr H. The adviser didn't estimate how much the LTA charge could be, but instead told Mr H that the possibility of an LTA excess tax charge didn't outweigh all of the other attractive features of transferring out, such as inheritability and flexibility. But I disagree, for the reasons I've already explained. It's fair and reasonable that this additional loss is covered by KMD as it won't be included in the usual DB transfer redress guidance.

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 H. But as I've said, KMD wasn't there to just transact what Mr H might have thought he wanted. Its role was to really understand what M 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 particular reasons which would justify a transfer and outweigh this. He was also likely to be subject to an LTA tax charge by transferring out. Mr H shouldn't have been advised to transfer out of his DB scheme just to have flexibility and control he didn't need, and the potential for higher death benefits wasn't worth giving up the guarantees associated with his DB scheme. It also wasn't worth the risk of him incurring an LTA tax charge.

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

Of course, I have to consider whether Mr H would've gone ahead anyway, against KMD's advice. KMD has reiterated its argument that this is the case here. It says Mr H had already contacted another financial adviser and obtained a CETV before speaking to KMD, and he'd told KMD he wanted a guarantee he and his wife could transfer their DB pension benefits into personal pensions.

I've considered this carefully, but I'm not persuaded that Mr H would've insisted on transferring out of the DB scheme, against KMD's advice. I say this because I think Mr H was an inexperienced investor with a broadly medium attitude to risk and this pension accounted for the majority of his retirement provision. So, if KMD 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 having flexibility, control and potentially better death benefits 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 him or in his best interests. If KMD had explained that Mr H could meet all of his genuine 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.

It's also clear that immediately after being given the advice, Mr H raised concerns about the impact of the transfer on his LTA. So, if the adviser had given clear advice, that transferring could lead him to pay a higher LTA charge in the future, I think he would've accepted the advice to remain in the DB scheme.

In light of the above, I think KMD should compensate Mr H 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 KMD to put Mr H, as far as possible, into the position he would now be in but for KMD's unsuitable advice to transfer his DB pension. I consider Mr H would have most likely remained in his DB scheme if suitable advice had been given.

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.

He has chosen not to wait for any new guidance to come into effect to settle his complaint.

I am satisfied that a calculation in line with FG17/9 remains appropriate and, if a loss is identified, will provide fair redress for Mr H.

KMD must therefore undertake a redress calculation in line with the regulator's pension review guidance as updated by the Financial Conduct Authority in its Finalised Guidance 17/9: Guidance for firms on how to calculate redress for unsuitable DB pension transfers.

For clarity, I understand that Mr H has not yet retired and has no plans to do so at present. So, compensation should be based on his normal retirement age of 60, 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 H's acceptance of my final decision.

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

If the redress calculation demonstrates a loss, the compensation 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.

KMD should also pay Mr H compensation for future LTA charges. It's impossible to say how much additional LTA charges Mr H will have to pay by transferring out of the DB scheme. It will depend on many factors like when Mr H will die, how he will use his pensions and what returns he will achieve in his personal pension and is highly complex. So I recognise that no award in this regard will be perfect, and Mr H's actual LTA charges might be higher or lower in future.

In my provisional decision, I said that if both parties preferred, KMD could give Mr H an undertaking to pay any LTA charges he incurs in the future (not taking into account further contributions or new pension arrangements). Neither Mr H nor KMD expressed a preference for this.

Given this, I think it's fair and reasonable to make an award now and bring finality to this complaint and certainty for the benefit of both parties. So I'm asking KMD to calculate Mr H's LTA charges using the following assumptions:

I can see that at age 55 Mr H crystalised £400,000 of his pension. However, he's currently not retired. I don't know when he will retire. For the purposes of this calculation KMD should assume that Mr H will be retiring at 60 like he originally planned and will not take further benefits until then. It should then be assumed he'll take TFC of 25% of his remaining drawdown fund at age 60 and an annual gross income until age 75. Again, I don't know how much income Mr H will take. I think a reasonable assumption is what he could have taken from the DB scheme (after TFC). This sum wasn't recorded at the time of the advice. Given that the full income was around £42,000, I think a reasonable assumption would be an annual gross income of £30,000 in the circumstances.

I considered the regulator's middle projection rate of 5% and what the suitability report says will be the recommended plan's charges of 0.99% (0.27% platform charge plus 0.72% fund manager charge). So, I think an assumed net growth rate of 4.01% per year should be applied to the value of Mr H's pension at the date of calculation every year until age 75.

The LTA might be higher than it is now or lower. In the more recent past, it increased on a regular basis, but it is currently frozen until 2026. I think for the purpose of this calculation and given the uncertainties in this area, it should be assumed that the LTA remains the same as it is now (£1,073,100).

Using the assumptions above, KMD will be able to establish when Mr H would exceed his LTA and what the charges are at this point. At age 75, there will be another test of benefits against the LTA charge which should be factored in.

The charges will be 25% of the sum he crystalizes before age 75 exceeding his LTA and again at age 75. This represents Mr H's loss. So, this is the amount Mr H should be compensated for. However, it needs to be considered that the amount being paid to Mr H now can be reinvested and achieve growth until age 75. So, the loss amount can be discounted with the same 4.01% rate for the time between Mr H's 75th birthday and the date of settlement.

The payment resulting from all the steps above is the 'compensation amount'. This amount must where possible be paid to Mr H within 90 days of the date KMD 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 KMD to pay Mr H.

Income tax may be payable on any interest paid. If KMD deducts income tax from the interest, it should tell Mr H how much has been taken off. KMD 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.

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 KMD 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 uphold this complaint and require KMD Associates 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 additionally require KMD Associates 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 only require KMD Associates 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 KMD Associates Ltd pays Mr H the balance. I additionally recommend any interest calculated as set out above on this balance to be paid to Mr H.

If Mr H accepts my final decision, the money award becomes binding on KMD Associates Ltd.

My recommendation would not be binding. Further, it's unlikely that Mr H can accept my 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 any final decision.

KMD Associates Ltd should provide details of its calculations to Mr H in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 21 March 2023.

Ailsa Wiltshire
Ombudsman