DRN-4040666

The complaint

Mr A has appointed a law firm to represent him in this complaint. For ease of reading, I've referred to the representative's comments as being Mr A's.

Mr A complains that an Appointed Representative of The On-Line Partnership Limited ("TOLP") wrongly advised him in June 2018 to transfer the value of his benefits built up in his former employer's defined contribution workplace pension scheme ("WPS") to an existing Personal Pension Plan ("PPP") provided by Prudential. He believes that the transfer was unsuitable because the PPP is likely to provide a lower level of retirement income than would've been provided by his former employer's WPS.

What happened

The events leading up to this complaint were set out in detail by our investigator in her assessment which she provided to both Mr A and TOLP. I don't intend to repeat here what our investigator stated but will instead provide a summary.

Mr A was a member of his former employer's WPS between January 2009 and May 2018. As at 14 June 2018, his benefits in the WPS were valued at £111,249.88. The money was invested equally between the Balanced Fund (50%) and the Schroder's Diversified Growth Fund (50%). The WPS didn't support adviser charging nor would it facilitate Flexi-Access Drawdown ("FAD") when Mr A accessed benefits.

On 28 June 2018, TOLP issued its suitability report to Mr A recommending that he transfer the value of his benefits in the WPS to an existing PPP provided by Prudential. Mr A's circumstances and objectives were recorded in June 2018 as follows:

- He was aged 54, in good health and married with three children, all of whom were financially independent;
- He had recently been made redundant by the long-term former employer linked to his WPS after it had decided to close a factory. His wife was employed as a part-time cleaner;
- As part of his redundancy package he received a large payment of about £73,000, the majority of which was invested in his WPS plan. He retained £30,000 tax-free and intended to use this as an 'income' to meet living costs in the short-term while he took a break from work;
- His non-pension assets comprised his residential home valued at about £200,000;
- His debts comprised a part repayment and part interest-only mortgage of about £90,000 on his residential home which was due to be repaid in 2029. He didn't have any other debts;
- He had an existing PPP provided by Prudential (the subject of this complaint) which had been set up by TOLP in 2017 to specifically receive a transfer value of

£220,842.23 in connection with Mr A's preserved benefits in the same former employer's defined benefits pension scheme (the advice about which this Service has previously considered and upheld under a separate complaint reference); and

- He had a *'Balanced'* risk profile – this was based on a risk profile assessment carried out by TOLP in January 2017.

TOLP recorded Mr A's objectives in June 2018, summarised as follows:

- Following his redundancy in May 2018, he wanted to take a break from work for up to a year during which he would use £30,000 of his redundancy payment as a source of 'income' to meet living costs. Then, after a year, he wanted to start part-time work and possibly supplement that income by drawing pension benefits flexibly;

- Repaying his mortgage was a major priority;

- He wanted all his pensions to be held together under a single plan; and

- He wanted to receive ongoing financial advice provided by TOLP.

To achieve these objectives, TOLP recommended that Mr A transfer the value of his benefits in the WPS to his existing PPP provided by Prudential. It recommended that the value of his PPP be invested in the '*PruFund Growth*' fund to align with his *'Balanced'* risk profile. The costs associated with TOLP's recommendation were stated as follows:

Initial charge

- 1.5% (or £1,668) initial adviser charge, payable to TOLP based on the transfer value

Ongoing annual charges based on the PPP fund value

- 0.50% ongoing adviser charge, payable to TOLP
- 0.79% fund charge and additional expenses, payable to Prudential
- 0.35% annual service charge for PPP, payable to Prudential

Mr A accepted the recommendation following which the transfer was completed.

This complaint

Mr A complained to TOPL that it wrongly advised him in June 2018 to transfer the value of his benefits built up in his former employer's WPS to his existing PPP provided by Prudential. He didn't think the transfer was in his bests interests and had caused him to suffer a financial loss.

TOPL didn't uphold this complaint. It said the transfer to the PPP was suitable and met Mr A's needs because it enabled him to consolidate his pension arrangements into a single plan, provided a wider selection of investment options through Prudential, provided the option to withdraw tax-free cash only, offered FAD and facilitated adviser charging, none of which would've been available had he maintained benefits in the WPS. In its view, remaining in the WPS wouldn't have met Mr A's needs and so – to achieve his objectives – he was compelled to transfer to a product, such as the PPP it recommended, to enable him to achieve his objectives.

Our investigator had a different view and recommended that this complaint be upheld on the basis that there wasn't any credible reason for Mr A to transfer at that time. She acknowledged that Mr A was likely attracted to the ability to access benefits flexibly but, given that he didn't require immediate flexible benefits, didn't think he needed to transfer at that time and so should've been advised to defer any decision to transfer. In the investigator's view, given the lower charges, Mr A should've been advised to maintain benefits in his WPS until such time as he required immediate access at which point a transfer could be properly considered.

To put things right, the investigator recommended that TOPL pay any compensation due to Mr A on the basis that he maintained benefits in his WPS. She stated that if the previous provider of the WPS was unable to provide a notional fund value, then compensation should be on the basis that Mr A would've invested broadly in line with: 50% in the FTSE UK Private Investors Income Total Return Index and 50% based on the average rate from fixed rate bonds. The investigator also recommended that TOLP refund to Mr A any adviser fees he paid in connection with the recommendation plus simple interest at 8% a year from the date the fees were paid to the date of settlement.

Mr A didn't express any view on whether he accepted our investigator's opinion and recommended remedy. TOLP submitted additional comments. In summary, it remained satisfied that its advice in June 2018 was suitable and enabled Mr A to achieve his recorded objectives. It noted that Mr A had flexibly accessed his PPP in April 2019 to help repay the interest-only part of his mortgage and to provide flexible income through FAD – and that he wouldn't have been able to achieve these outcomes had he maintained benefits in the WPS since it didn't allow members to access benefits flexibly.

Our investigator considered the additional comments received from TOLP but wasn't persuaded to change her opinion. Since agreement couldn't be reached, this complaint has been referred to me, an ombudsman, 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.

In deciding this complaint I've taken into account the law, any relevant regulatory rules, guidance and good industry practice at the time. I've also carefully considered the submissions made by Mr A and TOLP. Where the evidence is unclear, or there are conflicts, I've made my decision based on the balance of probabilities. In other words I've looked at what evidence we do have, and the surrounding circumstances, to help me decide what I think is more likely to, or should, have happened.

I'd like to clarify that the purpose of this final decision isn't to repeat or address every single point raised by Mr A or TOLP. If I haven't commented on any specific point, it's because I don't believe it's affected what I think is the right outcome. I've considered all the evidence afresh. Having done so, I've reached the same conclusion as our investigator for broadly the same reasons. I've explained why below.

<u>The regulator's suitability rules and guidance</u>

TOLP was authorised and regulated by the Financial Conduct Authority ("FCA") at the time it advised Mr A. So when it advised him on his retirement planning it was required to adhere to the suitability rules and guidance in the Conduct of Business Sourcebook ("COBS") section in the FCA's Handbook.

Primarily, TOLP was required under COBS 2.1.1R to *"act honestly, fairly and professionally* *in accordance with the best interests of its client"* in its dealings with Mr A. The suitability rules and guidance that applied when TOLP provided its recommendation to Mr A were set out in COBS 9. The purpose of the FCA's rules and guidance is to ensure that regulated businesses take reasonable steps to provide advice that's suitable for their clients' needs and to ensure they're not inappropriately exposed to a level of risk beyond their investment objective and risk profile. In order to ensure this was the case, and in line with the requirements in COBS 9, TOLP needed to gather necessary information for it to be confident its advice met Mr A's objectives and that it was suitable. Broadly speaking, TOLP had to undertake a "fact find" process in order to achieve this.

In addition to the requirements set out in COBS 9, the then regulator, the Financial Services Authority, issued a report in December 2008 titled *"Quality of advice on pension switching"* which I think was relevant when TOLP advised Mr A in June 2018. The report summarised the findings of the regulator's thematic review on the quality of advice given to individuals since pensions A-day on 6 April 2006 to switch the value of their pensions into a PPP. The regulator stated:

> *"We assessed advice as unsuitable when the outcome was the customer switching into one of the following:*
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> *• A pension incurring extra product costs without good reason (this outcome involved assessing cases where, for example, the reason for the switch was for investment flexibility, but this was not likely to be used; the reason was fund performance, but there was no evidence the new scheme was likely to be better; or the reason was flexibility of a drawdown option, but there was no evidence that this option was needed).*
>
> *• A pension that was more expensive than a stakeholder pension, but a stakeholder pension would have met the customer's needs.*
>
> *• A more expensive pension in order to consolidate different pension schemes, but where the extra cost was not explained or justified to the customer.*
>
> *• A new pension and the customer had lost benefits from their ceding pension (for example, guaranteed annuity rates) without these being explained or justified.*
>
> *• A pension that did not match the customer's attitude to risk and personal circumstances.*
>
> *• A pension where there was the need for ongoing advice, but this had not been explained, or offered, or put in place."*

So, the regulator clearly outlined what should be considered and stated cost was a factor as well as suitable other reasons for the transfer.

Was TOLP's advice suitable?

WPSs are generally less expensive than personal arrangements such as PPPs since the sponsoring employer typically covers some or all of the costs and/or is able to negotiate lower investment costs with providers and fund managers. In addition, most WPSs provide access to a wide range of funds that meet most individuals' risk profiles and investment objectives. So, in my view, there needs to be a compelling reason why an individual would transfer out of a WPS.

TOLP's recommendation to transfer from the WPS to the PPP entailed the following costs:

- 1.5% initial adviser charge, payable to TOLP based on the transfer value
- 0.50% pa ongoing adviser charge, payable to TOLP
- 0.79% pa fund charge and additional expenses, payable to Prudential
- 0.35% pa annual service charge for PPP, payable to Prudential

The suitability report stated that the PPP had a *"clear and competitive charging structure"* and that the ongoing cost, including advice, would be 1.64% pa of the fund value. However, neither the charging structure of the WPS nor the fact that it was less expensive than the recommended PPP were explicitly stated in the suitability report. The only indication provided to Mr A that the WPS had lower costs was in the following snapshot of the projected fund values at age 65 based on three different assumed growth rates:

Projected Fund (Paid Up) at proposed age of 65

	Assumed Growth Rates		
	-0.5%	**2.4%**	**5.4%**
Existing Scheme*	**£99,606**	**£135,369**	**£182,390**
Reduction in Yield	0.6%	0.6%	0.6%
Prudential Retirement Account	**£87,400**	**£118,000**	**£160,000**
Rate of Return Required from Prudential	0.74% (+1.24%)	3.7% (+1.3%)	6.66% (+1.26%)
The effect this will have on the fund if moved to Prudential	-12.18%	-12.18%	-12.18%
Reduction in Yield if moved to Prudential	1.8%	1.9%	1.9%

It was noted that the projections for the *"Existing Scheme"* or WPS had been *"system generated using a 0% Product AMC, 0.56% Fund AMC".* Mr A's money in the WPS was invested equally between two funds which, according to the WPS investment guide dated November 2017, had the following AMC:

- Balanced Fund 0.361%
- Schroder's Diversified Growth Fund 0.75%

I calculate the blended AMC to be 0.56%. So I'm satisfied that the correct AMC was used in the comparison.

These projections showed that, based on the same assumed growth rates, the WPS would provide a higher fund value than the recommended PPP at age 65 due to lower charges – and that Mr A would likely be worse off by transferring. But it required Mr A, who was an inexperienced investor, to read and understand that the difference in projected fund values was due to the fact that the WPS had lower charges that the PPP.

Notwithstanding this point, the projections were to age 65 despite the fact it was recorded Mr A intended to access benefits before then, probably around age 55. This is relevant because the projected growth in the short term under the PPP was unlikely to offset the impact of the higher charges and cost of the initial advice itself, further undermining the case for a transfer at that time.

I accept that increased charges don't automatically make the advice to transfer unsuitable. But the regulator stated there needs to be a good reason for the switch to justify these. And in Mr A's case, I'm not persuaded there was a compelling reason why it was suitable for him to transfer away from the WPS at that time given he wasn't seeking to immediately access benefits. I say this because I think the decision to transfer should've been deferred until there was more clarity about Mr A's plans. It was recorded that following his redundancy in May 2018, he wanted to take a break from work for up to a year during which he would use £30,000 of his redundancy payment as a source of 'income' to meet living costs. Then, after a year, he would aim to work part-time and possibly supplement that income by drawing pension benefits flexibly.

So I think it's fair to say that there was uncertainty regarding how long the £30,000 might last and his future plans about part-time employment, how much he might earn from that and when and how much money he'd need to draw from his pension.

Therefore, I don't believe flexibility was a good enough reason to recommend a transfer at that time. I think any decision about transferring should've been delayed until there was clarity about his circumstances and then – at that point – obtain financial advice when his needs could be determined with greater accuracy. In the meantime, I think he should've maintained benefits in the WPS at a lower cost than the alternative PPP recommended by TOLP. It's my view that TOLP's recommendation led to Mr A incurring additional costs without good reason. I consider that it was unlikely investment performance could be improved to a sufficient extent in the PPP to outweigh the initial advice charge and higher ongoing charges.

TOLP has stated that Mr A flexibly accessed his PPP in April 2019 to help repay the interest-only part of his mortgage and to provide flexible income through FAD. I think it made this point to support its position that its advice in June 2018 was suitable. But I think this actually undermines its position. Firstly, it shows that it was inappropriate for TOLP to run the projected fund values to age 65 when it was clear he would likely access benefits sooner as was proved to be the case. And the fact that Mr A didn't access benefits until April 2019 supports my view that there wasn't any compelling reason to recommend a transfer in June 2018 since it was clear that he didn't require immediate access at that time.

I want to address TOLP's consideration of stakeholder pensions. It had a regulatory requirement to consider stakeholder pensions as a possible destination to receive the transfer since the charges on these plans are capped. The adviser stated in the suitability report, *"I have not recommended a stakeholder pension as they offer less flexibility in terms of fund choice and would not offer the required flexibility in terms of drawdown options. Nor would they offer the robust investment processes you were looking for."*

I have concerns about the reasons why TOLP dismissed a stakeholder pension as a viable option for Mr A. I'm not sure what was meant by *"robust investment processes"* and why Mr A was apparently seeking this. In my view, the reference to stakeholder pensions not offering flexibility in terms of fund choice and FAD is misleading. Stakeholder plans typically offer a wide range of funds that are suitable for most individuals' risk profiles and objectives. The evidence shows that Mr A was an inexperienced investor whose needs likely would've been met by the sort of funds typically available under lower-cost stakeholder pensions. In addition, I understand that some stakeholder products offer FAD. So I think it's likely a stakeholder pension would've met Mr A's needs. I'm not convinced that TOLP properly considered stakeholder pensions in its analysis. But in any event, for the reasons explained above, I don't think Mr A needed to transfer at that time.

The adviser noted in the suitability report that he had discussed with Mr A the option of leaving any decision about a possible transfer until he was aged 55. However, it was stated that in June 2018 Mr A wanted to keep all of his pension benefits under one plan for simplicity and to transfer to his existing PPP. And so he didn't want to consider the option of maintaining benefits in the WPS. I don't think consolidation was a justifiable reason to incur additional costs at that time. In any event, the reason why Mr A had that existing PPP was because TOLP had advised him to start it in 2017 specifically to receive a transfer value of

£220,842.23 in connection with his preserved benefits in the same former employer's defined benefits pension scheme – the suitability of that advice was later assessed by this Service and found to be unsuitable, meaning that Mr A shouldn't have been sold the PPP in 2017.

Conclusion

I'm not persuaded that TOLP demonstrated why it was suitable advice in June 2018 for Mr A to transfer away from the WPS. The transfer led to additional costs without good reason. I think what was important at that stage, bearing in mind Mr A was then aged 54, was to seek – as much as possible – to preserve and maximise the returns (at the lowest cost) from his existing benefits in the WPS until such time as he required immediate access when his needs could be determined with greater accuracy. I don't think TOLP acted in Mr A's best interests.

Putting things right

My aim is that Mr A should be put as closely as possible into the position he would probably now be in if he had been given suitable advice.

In my opinion, properly advised, Mr A would've maintained benefits in his former employer's WPS. I'm satisfied what I've set out below is fair and reasonable, taking this into account and given his circumstances when he invested. What I've set out below is in line with the remedy recommended by our investigator.

To compensate Mr A fairly, TOLP must:

- Compare the performance of Mr A's investment with the notional value if it had remained in his former employer's WPS. If the actual value is greater than the notional value, no compensation is payable. If the notional value is greater than the actual value, there is a loss and compensation is payable.

- Also pay any interest set out below.

- If there's a loss, TOLP should pay into Mr A's PPP, to increase its value by the amount of the compensation and any interest. TOLP's payment should allow for the effect of charges and any available tax relief. TOLP shouldn't pay the compensation into the PPP if it would conflict with any existing protection or allowance.

- If TOLP is unable to pay the compensation into Mr A's PPP, it should pay that amount direct to him. But had it been possible to pay into the PPP, it would've provided a taxable income. Therefore, the compensation should be reduced to notionally allow for any income tax that would otherwise have been paid. This is to ensure the compensation is a fair amount – it isn't a payment of tax to HMRC, so Mr A won't be able to reclaim any of the reduction after compensation is paid.

- The *notional* allowance should be calculated using Mr A's actual or expected marginal rate of tax at his selected retirement age. I've decided that Mr A is likely to be a basic rate taxpayer in retirement, so the reduction would equal 20%. However, if Mr A would've been able to take a tax-free lump sum, the reduction should be applied to 75% of the compensation, resulting in an overall reduction of 15%.

- Repay the adviser's fees together with simple interest at 8% a year, from the date the fees were paid to the date of this final decision. If the above comparison shows that no compensation is payable, the difference between the actual value and the notional value can be offset against the fees with interest.

- Provide the details of the calculation to Mr A in a clear, simple format.

Income tax may be payable on any interest paid. If TOLP consider that it's required by HM Revenue & Customs to deduct income tax from that interest, it should tell Mr A how much it's taken off. TOLP should also give Mr A a tax deduction certificate in respect of interest if Mr A asks for one, so he can reclaim the tax on interest from HM Revenue & Customs if appropriate.

Portfolio name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Prudential PPP	Still exists and liquid	Notional value from previous WPS (if notional value is not available then for half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds)	Date of transfer-in to Prudential PPP	Date of this final decision	8% per annum simple from date of this final decision if TOLP doesn’t settle within 28 days of receipt of Mr A’s acceptance

Actual value

This means the actual amount payable from the investment at the end date.

Notional Value

This is the value of Mr A’s investment had it remained in his former employer’s WPS until the end date. TOLP should request that the previous provider calculate this value.

Any withdrawal from the funds that were transferred from the WPS to the PPP should be deducted from the notional value calculation at the point it was actually paid so it ceases to accrue any return in the calculation from that point on. If there were a large number of regular payments, to keep calculations simpler, I’ll accept if TOLP total all those payments and deduct that figure at the end to determine the notional value instead of deducting periodically.

If the previous provider is unable to calculate a notional value, TOLP will need to determine a fair value for Mr A’s investment instead, using this benchmark: For half the investment: FTSE UK Private Investors Income Total Return Index; for the other half: average rate from fixed rate bonds. The adjustments above also apply to the calculation of a fair value using the benchmark, which is then used instead of the notional value in the calculation of compensation.

Why is this remedy suitable?

I’ve chosen this method of compensation because:

- Mr A wanted income with some growth with a small risk to his capital.
- If the previous provider is unable to calculate a notional value, then I consider the measure below is appropriate.
- The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to his capital.
- The FTSE UK Private Investors Income total return index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is made up of a range of indices with different asset classes, mainly UK equities and government bonds. It’s a fair measure for someone who was prepared to take some risk to get a higher return.
- I consider that Mr A's risk profile was in between, in the sense that he was prepared to take a small level of risk to attain his investment objectives. So, the 50/50 combination would reasonably put Mr A into that position. It doesn’t mean that Mr A would’ve invested 50% of his money in a fixed rate bond and 50% in some kind of index tracker investment. Rather, I consider this a reasonable compromise that broadly reflects the sort of return Mr A could’ve obtained from investments suited to his objective and risk attitude.

My final decision

I uphold Mr A’s complaint and require The On-Line Partnership Limited to pay him compensation as set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr A to accept or reject my decision before 24 August 2023.
Clint Penfold
Ombudsman