DRN-4063775

The complaint

Mr D has complained that CST Wealth Management Limited (CST) gave him unsuitable advice to transfer his defined benefits from his occupational pension scheme (OPS) – the British Steel Pension Scheme (BSPS) – to a Personal Pension Policy (PPP).

What happened

The investigator who considered this matter set out the background to the complaint in his assessment of the case. I'm broadly setting out the same background below, with some amendments for the purposes of this decision.

In March 2016, Tata Steel UK Ltd announced that it would be examining options to restructure its business, including decoupling the BSPS from the company. The consultation with members referred to possible outcomes regarding their preserved benefits, 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 defined benefit pension schemes when their employer becomes insolvent. The BSPS was closed to further benefit accrual from 31 March 2017.

In May 2017, the Pension Protection Fund (PPF) made the announcement that the terms of a Regulated Apportionment Arrangement (RAA) had been agreed. That announcement said that, if risk-related qualifying conditions relating to funding and size could be satisfied, a new pension scheme sponsored by Mr D's employer would be set up – the BSPS 2.

This was, however, intended to receive deferred benefits only. The main defined benefit OPS had been replaced by a new defined contribution scheme. The existing scheme was due to be closed in the near future, with the options being set out in a subsequent letter in October 2017 for deferred members to either transfer their benefits to the successor scheme, BSPS 2, the PPF or into a private arrangement, such as a PPP.

A fact find was completed to understand Mr D's circumstances and objectives at the time. Details were also taken of his partner. The key points from this are summarised below:

- He was 33 and engaged to his partner (of the same age).
- He was in good health.
- His income was £30,000 pa, or £2,000 net pm.
- He owned his home, which had a mortgage of £65,000.
- He had savings of £13,000, which were earmarked for his wedding.

- He had an outstanding loan and car finance.
- His monthly expenditure totalled £1,500.
- He was paying 6% to his group personal pension and the employer was paying 10%.
- He was also entitled to another defined benefit pension of around £1,000 pa.

A pension transfer questionnaire was completed. From that questionnaire, Mr D expressed the sentiment that there were many “unanswered questions” with the BSPS, that he was too far away from retirement to decide on lump sum needs, and that he didn’t anticipate retiring early, but would like the flexibility to do so if circumstances changed.

His capacity and tolerance for loss was agreed as “cautious”. He didn’t mind a reasonable degree of risk, but handwritten notes recorded that he wasn’t a high risk taker. An attitude to risk (ATR) questionnaire noted that Mr D had never invested before. The results of the questionnaire indicated an ATR of “highest-medium”.

CST complete a transfer value analysis (TVAS) based on the cash equivalent transfer value (CETV) of £60,832.

It estimated the scheme benefits at age 60 to be a full pension of £4,406 pa or a lump sum of £21,136 and reduced pension of £3,170 pa. The critical yields to match those benefits were 5.99% and 5.31% respectively.

The TVAS set out that if Mr D drew an income from a personal pension which was equivalent to the benefits of the BSPS, then based on an annual return of 5%, his fund would last until at least age 116.

CST set out its recommendations in a suitability letter dated 10 November 2017. It advised Mr D to transfer to a PPP, noting his primary objectives as follows:

- He wanted to secure the generous transfer value.
- He wanted to avoid a transfer into the PPF.
- He wanted the potential for capital growth over the next 30 years.
- He wanted control over his pension, due to mistrust of the scheme.

CST recommended that Mr D invest the transfer value in the “Governed Portfolio 4”, which was graded as a moderately cautious/balanced fund. Mr D accepted the recommendation and proceeded with the transfer.

Mr D complained to CST in June 2022, but CST declined to uphold the complaint.

Dissatisfied with the response, Mr D referred the matter to this service.

Having considered the complaint, our investigator thought that it should be upheld. He said the following in summary:

- The regulator’s guidance, when considering a transfer of defined benefits, was that it should be presumed to be unsuitable unless it could be clearly demonstrated that it was in an individual’s best interests.

- The advice had been after the regulator had given instructions in final guidance FG17/9 as to how businesses could calculate future “discount rates” for complaints about transfers which were being upheld. Prior to that, this service was publishing information with which businesses could calculate future “discount” rates.

- Whilst businesses weren't required to use these when giving advice, they nevertheless provided a useful guide as to the kinds of returns deemed feasible at the time of the advice.

- The discount rate for the 30 or so years left to retirement was 4.6% pa and the regulator's mid band growth projection was 5% pa. Taking into account Mr D's attitude to risk and the recommended fund, and given the critical yields required simply to match the scheme benefits, it was unlikely that the scheme benefits could be bettered through transferring.

- Mr D may have been keen on having flexibility of income, but he still had around 27 years before prospective retirement and so wouldn't have known what the shape of his retirement benefits would need to be at the time of the advice. There was much scope for his circumstances (he was soon to be married and may have started a family) - and his career - to have changed in the intervening period.

- The accrued fund in the defined contribution plan would likely be able to meet any requirements for flexibility of income.

- Lump sum death benefits, and the legacy that this may provide for his family, might have been attractive to Mr D, but the advice needed to be given in his best interests – which was his own financial security in retirement.

The investigator recommended that CST undertake a loss calculation in accordance with the regulator's guidance (FG 17/9) for such complaints – and on the basis that Mr D would have opted to join the BSPS 2.

But the investigator also noted the regulator's consultation on a revised methodology and enquired of Mr D as to whether, if the complaint was upheld, his preference would be to have a loss calculation undertaken on the existing basis, or to await the new methodology for defined benefit transfer redress calculations.

He said that any redress should in the first instance be paid to Mr D's pension plan, but if this wasn't possible, it should be paid directly to Mr D, with a notional deduction for the (assumed basic rate) income tax he would have paid on the pension benefits.

Mr D accepted the investigator's findings and confirmed that he'd like any redress to be calculated on the basis of the current methodology.

CST submitted no response on the merits of the case.

The investigator then wrote to both parties to confirm that the FCA had developed a BSPS-specific redress calculator to calculate redress for cases which were included in the BSPS consumer redress scheme. But, he said, the FCA was also encouraging businesses to use the calculator for non-scheme cases.

The investigator further said that, when issuing my decision, I may require CST to use the FCA's BSPS-specific calculator to determine any redress due to Mr D.

The investigator said that, if either party didn't think it was appropriate to use the BSPS-specific redress calculator in the circumstances of Mr D's complaint, they should let him know by 5 June 2023.

CST confirmed that it would be using the BSPS-specific redress calculator if an ombudsman upheld the complaint.

The matter has now been referred to me for review.

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.

When considering what's fair and reasonable, and in accordance with the Financial Services and Markets Act 2000 (FSMA) and DISP, I need to take into account relevant: law and regulations; regulators' rules, guidance and standards, and codes of practice; and, where appropriate, what I consider to have been good industry practice at the time.

The applicable guidance, rules, regulations and requirements

This isn't a comprehensive list of the guidance, rules and regulations which applied, but provides useful context for my assessment of the business' actions here.

Within the FCA's handbook, COBS 2.1.1R required a regulated business *to "act honestly, fairly and professionally in accordance with the best interests of its client".*

The FCA's suitability rules and guidance that applied at the time CST advised Mr D were set out in COBS 9. The purpose of the rules and guidance is to ensure that regulated businesses, like CST, take reasonable steps to provide advice that is 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 COBS 9.2.2R, CST needed to gather the necessary information for it to be confident that its advice met Mr D's objectives and that it was suitable. Broadly speaking, this section sets out the requirement for a regulated advisory business to undertake a "fact find" process.

There were also specific requirements and guidance relating to transfers from defined benefit schemes – these were contained in COBS 19.1.

COBS 19.1.2 required the following:

"A firm must:

(1) compare the benefits likely (on reasonable assumptions) to be paid under a defined benefits pension scheme or other pension scheme with safeguarded benefits with the benefits afforded by a personal pension scheme, stakeholder pension scheme or other pension scheme with flexible benefits, before it advises a retail client to transfer out of a defined benefits pension scheme or other pension scheme with safeguarded benefits;

(2) ensure that that comparison includes enough information for the client to be able to make an informed decision;

(3) give the client a copy of the comparison, drawing the client's attention to the factors that do and do not support the firm's advice, in good time, and in any case no later than when the key features document is provided; and

(4) *take reasonable steps to ensure that the client understands the firm's comparison and its advice."*

Under the heading *"Suitability"*, COBS 19.1.6 set out the following:

"When advising a retail client who is, or is eligible to be, a member of a defined benefits occupational pension scheme or other scheme with safeguarded benefits whether to transfer, convert or opt-out, a firm should start by assuming that a transfer, conversion or opt-out will not be suitable. A firm should only then consider a transfer, conversion or opt-out to be suitable if it can clearly demonstrate, on contemporary evidence, that the transfer, conversion or opt-out is in the client's best interests."

COBS 19.1.7 also said:

"When a firm advises a retail client on a pension transfer, pension conversion or pension opt-out, it should consider the client's attitude to risk including, where relevant, in relation to the rate of investment growth that would have to be achieved to replicate the benefits being given up."

And COBS 19.1.8 set out that:

"When a firm prepares a suitability report it should include:

(1) a summary of the advantages and disadvantages of its personal recommendation;

(2) an analysis of the financial implications (if the recommendation is to opt-out); and

(3) a summary of any other material information."

As set out above, the starting assumption for a transfer from a defined benefit scheme is that it is unsuitable. So, CST should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr D's best interests.

Having considered the above and the evidence in this case, I've decided to uphold the complaint for broadly the same reasons set out by the investigator.

- The TVAS report which CST was required to carry out noted that the critical yield - how much Mr D's pension fund would need to grow by each year in order to provide the same benefits as his defined benefit scheme – was 5.99% to match the full pension he'd have been entitled to under the scheme at age 60. Or to match the maximum tax-free cash and reduced pension the scheme would provide at that age, it was 5.31%.

- Given Mr D's recorded "highest-medium" attitude to risk, the discount rate of 4.6% for the number of years until Mr D was 60, and the regulator's middle projection rate for growth (5% pa), I think Mr D was more likely than not to receive pension benefits, from age 60, of a lower value that those he'd have been entitled to under the BSPS 2 (or the PPF) by transferring and investing in line with that attitude to risk.

- As set out in the suitability report, at the time of the advice Mr D envisaged working until his normal retirement date. Early retirement may well have been appealing to Mr D, as it might reasonably be appealing to a great many people, but as noted by the investigator, his circumstances may in any case have changed significantly between then and retirement. Mr D was planning to marry, and may well have had a family, which can of course impact upon retirement plans.

- Mr D may not have envisaged relying upon the scheme benefits to any great extent at the time, but they would have formed a valuable foundation of guaranteed income, to complement that which he would have received from his other defined benefit scheme, and later the state pension, upon which the flexibility which would be offered by the defined contribution accrual could then be based. He would by necessity be relying upon risk based returns from another 30 or so years of pension accrual within the replacement group personal pension arrangement.

- In terms of the alternative lump sum benefits a transfer offered to his family, the priority here was to advise Mr D about what was best for his retirement. And the existing scheme offered death benefits, by way of a spouse's (and dependants') pension, that could have been valuable to his wife to be and any subsequent family in the event of his death.

- And while the CETV figure would no doubt have appeared attractive as a potential lump sum, the sum remaining on death following a transfer was always likely to be different. As well as being dependent on investment performance, it would have also been reduced by any income Mr D drew in his lifetime. And so may not have provided the legacy that Mr D may have thought it would.

- The different death benefits available through a transfer didn't justify the likely decrease of retirement benefits for Mr D. And ultimately CST shouldn't have encouraged Mr D to prioritise the potential for alternative death benefits through a PPP over his security in retirement.

- Mr D may have legitimately held concerns about how his employer had handled his pension and the prospect of entering the PPF. But it was CST's role to objectively address those concerns. At the time of the advice, all signs pointed toward the BSPS 2 being established. But even if not, the PPF still provided Mr D with guaranteed income and the option of accessing tax-free cash. Mr D was unlikely to improve on these benefits by transferring. So, entering the PPF wouldn't have been as concerning as Mr D might have thought, and I don't think any concerns he held about this meant that transferring was in his best interest.

Overall, I can't see persuasive reasons as to why it was clearly in Mr D's best interest to relinquish his defined benefits and transfer them to a PPP. And I also haven't seen anything to persuade me that Mr D would have insisted on transferring, against advice to remain in the defined benefit scheme.

So, as with the investigator, I'm upholding the complaint as I think the advice Mr D received from CST was unsuitable.

Putting things right

As set out in the investigator's further comments relating to the BSPS-specific redress calculator, I consider that it would be appropriate to use that calculator here, given the BSPS-specific circumstances.

A fair and reasonable outcome would be for the business to put Mr D, as far as possible, into the position he would now be in but for the unsuitable advice. I consider Mr D would more likely than not have remained in the occupational pension scheme and opted to join the BSPS 2 if suitable advice had been given.

CST Wealth Management Limited 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.

CST Wealth Management Limited should use the FCA's BSPS-specific redress calculator to calculate the redress. A copy of the BSPS calculator output should be sent to Mr D and our service upon completion of the calculation.

Mr D hasn't yet retired, and cannot do so for many years. So compensation should be based on the scheme's normal retirement age, as per the usual assumptions in the FCA's guidance.

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

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

- calculate and offer Mr D redress as a cash lump sum payment,

- explain to Mr D 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 their redress prudently is to use it to augment their defined contribution pension

- offer to calculate how much of any redress Mr D receives could be augmented rather than receiving it all as a cash lump sum,

- if Mr D accepts CST Wealth Management Limited's offer to calculate how much of its redress could be augmented, request the necessary information and not charge Mr D for the calculation, even if he ultimately decides not to have any of its redress augmented,

and

- take a prudent approach when calculating how much redress could be augmented, given the inherent uncertainty around Mr D's end of year tax position.

Redress paid to Mr D as a cash lump sum will be treated as income for tax purposes. So, in line with DISP App 4, businesses may make a notional deduction to cash lump sum payments to take account of tax that consumers would otherwise pay on income from their pension.

Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to Mr D’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.

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.

Determination and money award: I require CST Wealth Management Limited to pay Mr D the compensation amount as set out above, up to a maximum of £160,000.

Recommendation: If the compensation amount exceeds £160,000, I would also recommend that CST Wealth Management Limited pays Mr D the balance.

If Mr D accepts this final decision, the award will be binding on CST Wealth Management Limited.

My recommendation wouldn’t be binding on CST Wealth Management Limited. Further, it’s unlikely that Mr D could accept my decision and go to court to ask for the balance. Mr D may want to consider getting independent legal advice before deciding whether to accept my final decision.

My final decision

My final decision is that I uphold the complaint and direct CST Wealth Management Limited to undertake the above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr D to accept or reject my decision before 11 December 2023.

Philip Miller
Ombudsman