

The complaint

Mrs Y complains about the advice given by KD Wright Financial Services Limited ('KDWFS') to transfer the benefits from her defined-benefit ('DB') occupational pension scheme to a self-invested personal pension ('SIPP'). She says the advice was unsuitable for her and believes this has caused a financial loss.

What happened

Mrs Y had deferred benefits in an occupational pension scheme. In September 2017, she was provided a statement, including the cash equivalent transfer value (CETV) of her benefits, which was £581,491.73.

In November 2017, she contacted KDWFS to discuss her pension and retirement planning. Mrs Y says KDWFS were recommended to her by a former colleague.

On 20 November 2017, KDWFS sent Mrs Y an analysis summary report. This report first set out KDWFS's understanding of Mrs Y's circumstances and objectives. It said Mrs Y was 55, in good health, married with one son who was not financially dependent. Mrs Y was employed full time earning £46,500. Mr Y was also employed and his earnings, including state pension he was receiving, were approximately £29,000. They owned their home with an outstanding mortgage of £157,000 (approximately 37% of the property value), with a remaining term of 20 years. They had savings and investments totalling approximately £41,000. And Mrs Y also held another pension from her current employer with a value of around £23,000.

KDWFS said Mrs Y didn't have a set retirement age in mind but may look to stop work around age 60. It said she was interested in repaying as much of her mortgage balance as she could now, to reduce outgoings as she didn't want this level of debt for a further 20 years. And it said she wanted to carry out some refurbishment work at home. So, she was interested in immediately accessing tax-free cash ('TFC'). And KDWFS said Mrs Y wanted full control over her pension and the flexibility to control how benefits were paid.

KDWFS noted Mrs Y was a 'cautious risk investor'. But said, in conversation, she had expressed an interest in holding some investments on a balanced risk basis and a small percentage on an aggressive basis.

The report then set out details of the existing scheme and concluded by recommending that Mrs Y transfer her benefits away from the DB scheme. It said the critical yield – the rate Mrs Y's pension fund would need to grow by each year in order to purchase equivalent benefits to those the DB scheme would provide at her retirement age – of 6.4% was potentially achievable. TFC could be taken to address Mrs Y's objective of paying down her mortgage without her having to begin drawing an income, unnecessarily. And by transferring the pension could be left as a lump sum in the event of her death – which KDWFS said Mrs Y liked. And while she'd be giving up a guaranteed income, KDWFS said Mrs Y believed the transfer value would provide her sufficient income in retirement.

The analysis report did not include a recommendation of a specific new pension

arrangement or reasons for choosing a particular provider. Despite this, application forms for a SIPP were supplied to Mrs Y with the adviser's declaration marked as having been completed on the same day as the report.

These forms appear to have been signed by Mrs Y on 28 November 2017, with forms to the DB scheme authorising the transfer, a request for the release of TFC and KDWFS' client agreement all also signed at the same time.

In December 2017, KDWFS sent Mrs Y a pension transfer report. This explained that KDWFS had noticed a discrepancy in the transfer value analysis ('TVAS') report it had previously carried out – which had included the calculation of the critical yield. So, this had been re-run. The report went on to say that the critical yield to provide equivalent benefits to the full pension the DB scheme could provide at the normal scheme retirement age was 10.03%. KDWFS said though that it still recommended a transfer from her DB scheme, for much the same reasons given previously. This report also included confirmation of KDWFS' recommendation of a SIPP provider and investment mix. And that KDWFS would provide ongoing servicing and support, for a fee. I understand the transfer went ahead in line with KDWFS' recommendation.

Mrs Y complained to KDWFS in 2022. She said was concerned that the advice might've been unsuitable for her as she had become aware of the regulator's stance on DB pension transfers. So, she wanted KDWFS to review the advice and compensate her if the advice was unsuitable.

KDWFS didn't uphold Mrs Y's complaint. It said Mrs Y had wanted to release tax-free cash from her pension to reduce her mortgage and other debts, provide lump sum death benefits for her son and to have control over the pension. So, it felt the advice it gave was suitable and that Mrs Y was made aware of the risks involved.

Mrs Y referred her complaint to our service. One of our Investigator's considered the complaint. He thought it should be upheld and that KDWFS should compensate Mrs Y for any loss the DB transfer had led to. He thought Mrs Y was always unlikely to improve on the benefits the DB scheme already guaranteed by transferring. And he didn't think Mrs Y had a compelling need for flexibility, alternative death benefits or to access TFC and so thought the recommendation wasn't in her best interests.

KDWFS disagreed. It said the transfer had allowed Mrs Y to meet her objectives, so it still considered that the advice was suitable.

The investigator wasn't persuaded to change their opinion, so the complaint was referred to me to make a final decision.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

I've 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 KDWFS'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.

Having considered all of this and the evidence in this case, I've decided to uphold the complaint for largely the same reasons given by the investigator.

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, KDWFS should have only considered a transfer if it could clearly demonstrate that the transfer was in Mrs Y's best interests. And having looked at all the evidence available, I'm not satisfied it was in her best interests.

Financial viability

When referring to financial viability, I mean how likely it is that Mrs Y would be better off in terms of the retirement income she would receive, by transferring. Because moving from a DB scheme to a personal pension exposed her pension to risk that she wasn't otherwise subject to. And given a pension's primary purpose is to provide for the income needs of the holder in retirement, whether Mrs Y would be better off in retirement as a result of a transfer is, in my view, a relevant consideration when looking at what was in her best interests.

KDWFS carried out transfer value analysis as required by the regulator, including the calculation of a critical yield. It noted in the documents from the time that the initial analysis contained discrepancies though, so this was re-done. The initial report put the critical yield at 6.74% and the updated report said this was 10.03%.

In response to the Investigator's opinion KDWFS said that the critical yield of 6.74% was before taking TFC. And 10.03% was after TFC had been taken. But that isn't supported by the TVAS report outlining the figure of 10.03%. This makes it clear that the calculation is based on the whole transfer value being invested and doesn't indicate it intends to replicate Mrs Y taking TFC. But this notwithstanding, I don't think either of the critical yield figures were likely to be achieved here.

The advice was given after the regulator gave instructions in Final Guidance FG17/9 as to how businesses could calculate future 'discount rates' in loss assessments where a complaint about a past pension transfer was being upheld. Prior to October 2017 similar rates were published by the Financial Ombudsman Service on our website. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, they provide a useful indication of what growth rates would have been considered reasonably achievable for a typical investor.

The relevant discount rate closest to when the advice was given which I can refer to was published by the Financial Ombudsman Service for the period before 1 October 2017 and was 3% per year for four full years to retirement – which would've been the case if benefits were drawn from the DB scheme at the normal retirement age of 60, based on Mrs Y's age at the time of the advice. I've kept in mind that the regulator's projection rates had also remained unchanged since 2014: 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, Mrs Y's recorded 'cautious' attitude to risk and also the term to retirement. There would be little point in Mrs Y giving up the guarantees available to her through her DB scheme only to achieve, at best, the same level of benefits outside the scheme. But here, given the critical yield figures, I think Mrs Y was likely to receive benefits of a substantially lower overall value than the DB scheme at retirement, as a result of investing in line with that attitude to risk.

KDWFS has said, in response to our Investigator's opinion, that Mrs Y had a 'split risk profile'. And while she intended to invest 50% of her pension fund cautiously, she was also willing for 40% to be invested on a balanced basis and for 10% to be invested aggressively. I'm conscious though that the DB scheme appears to have made up the majority of Mrs Y's retirement provisions, so she had a low capacity for loss. Which to me indicates she was likely to want to take more caution and so the 'cautious' attitude to risk mentioned does appear to be accurate. But in any event, even if she were instead a 'balanced' investor, I still don't think this meant she was likely to improve on the benefits the DB scheme guaranteed by transferring.

Of course financial viability isn't the only consideration when giving transfer advice. There might be other considerations which mean a transfer is suitable, despite providing overall lower benefits. I've considered this below.

Flexibility and access to tax-free cash

KDWFS has said that Mrs Y wanted access to TFC to reduce her mortgage and other debt (although there was nothing recorded in the recommendations about the level or duration of those other debts) and carry out some home improvements. It says she was concerned about having to service such a large debt (the mortgage) for twenty years, particularly bearing in mind that Mr Y was a good deal older than her – already drawing state pension. And transferring and accessing TFC was the only way of achieving this objective. It also said doing this meant they wouldn't pay as much in interest over the mortgage term, offsetting some of the reduction in pension benefits. And it added that Mrs Y was keen on having flexibility and being able to draw income how and when she wanted.

There was nothing recorded in either of the letters recommending a transfer about Mrs Y's expected income needs in retirement. So, while the idea of being able to draw income flexibly might've appealed to her, I can't see that she had a strong need for this. Or, bearing in mind I think that she was always likely to receive lower retirement benefits as a result of transferring, that this flexibility allowed her to better meet her retirement income needs. So, I don't think transferring to achieve flexibility was demonstrated to be in her best interests.

I also don't think, based on the information available, that transferring to repay a portion of her mortgage at that time was something that she needed to do. I've seen nothing to suggest that Mr and Mrs Y were having difficulty making their mortgage repayments or those relating to any other debts they held, or that they were behind with any of these. And Mrs Y, who earned the greater portion of their income, intended to continue working for another several years at least. And there is no suggestion that she and Mr Y would've had any issues with making repayments for the foreseeable future. So, reducing the mortgage

seems, at best, to have been an aspiration or a 'nice to have' rather than a genuine need. And KDWFS' role wasn't just to do what Mrs Y might've thought she wanted – its role was to assess all of the relevant information and circumstances and recommend what was in her best interests.

The DB scheme also allowed Mrs Y to draw TFC at retirement. So, as she and Mr Y appear to have been able to afford the mortgage repayments, it appears they could've continued to do so until the normal scheme retirement age. At which point, Mrs Y could've drawn TFC and used this to reduce the mortgage balance. And she would then have received a guaranteed escalating income, to support with the payment of any residual balance. This would've achieved her apparent aim of not having such a significant debt over such a long term, without sacrificing the guaranteed pension income she was entitled to. But KDWFS doesn't appear to have considered or analysed this alternative. It said, in the second recommendation report, it hadn't received commutation factors to determine what level of TFC the DB scheme could provide. But I'd argue it shouldn't have given advice until it had.

KSWFS has said that reducing the mortgage immediately meant their payments would be reduced, making a saving. And it is true that having a lower level of debt would normally produce an interest saving. But firstly, it wasn't made clear how much of the TFC would be used to reduce the mortgage. KDWFS said there was other debt to potentially be repaid and home improvements were also something Mrs Y was considering. But there were no figures recorded for how much would be used for these purposes. So, it was unclear how much the mortgage balance would be reduced by. KDWFS also didn't refer in the recommendation to any specific information about the mortgage payments – what these were, what they would be after a reduction of the balance or what penalties for early repayment might be incurred. And in turn there was no comparison of these figures to how Mrs Y's retirement income would be impacted. So, there is nothing to support that this would improve her position.

Taking all of this into account, I don't think I can reasonably say that transferring to achieve this objective was in Mrs Y's best interests. It doesn't seem to have been something she *needed* to do. And she was again always likely to be worse off in retirement by doing so.

Death benefits

KDWFS says that the lump sum death benefits available through a SIPP appealed to Mrs Y – as they could provide a legacy for her son. And it argues that the spouse's benefit the DB scheme offered was unlikely to be called upon, given Mr Y was a good number of years older than Mrs Y and their average life expectancies.

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 Mrs Y. But whilst I appreciate death benefits are important to consumers, and Mrs Y might have thought it was a good idea to transfer her DB scheme to a personal pension because of this, the priority here was to advise her about what was best for her retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think KDWFS explored to what extent Mrs Y was prepared to accept a lower retirement income in exchange for alternative death benefits.

The CETV figure would no doubt have appeared attractive as a potential lump sum. And I can see that KDWFS made reference in its pension transfer report to this being available in full as a lump sum. But I think that was misleading. Because its advice was based on this immediately being reduced by 25% and Mrs Y taking TFC. And the sum remaining on death following a transfer was dependent on investment performance and would've also been reduced by any income Mrs Y drew in her lifetime. Mrs Y was recorded as being in good

health, so there was nothing to suggest she was less likely to live until at least her average life expectancy. By which time, given this pension accounted for the majority of her retirement provisions, it is likely the fund would've been significantly depleted. So, the pension may not have provided the legacy that Mrs Y may have thought it would.

Furthermore, if Mrs Y genuinely wanted to leave a legacy for her family, and in particular her son, which didn't depend on investment returns or how much of her pension fund remained on her death, life insurance could've been explored. And, given she was in good health, this could've been a reasonable and affordable alternative. But KDWFS doesn't appear to have considered this, which I think would've been appropriate when thinking about what was in Mrs Y's best interests.

Overall, I don't think different death benefits available through a transfer to a SIPP justified the likely decrease of retirement benefits for Mrs Y.

Control

I think Mrs Y's desire for control over her pension benefits was overstated. From the information available I'm satisfied Mrs Y was not an experienced investor. And I cannot see that she had an interest in or the knowledge to be able to manage her pension funds on her own. So, I don't think that this was a genuine objective for Mrs Y – it was simply a consequence of transferring away from her DB scheme.

And although the information from the point of sale indicated that the DB scheme was in deficit, her former employer, which sponsored the scheme, was one of the largest financial institutions in the country. And I haven't seen anything to suggest the funding of the scheme was in a position such that Mrs Y should have genuinely been concerned about the security of her pension. So, I also don't think it was in her interests to transfer because of this.

Suitability of investments

KDWFS recommended that Mrs Y invest in particular managed funds through her SIPP. And, as part of her complaint, Mrs Y questioned if the investments were suitable. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Mrs Y, it follows that I don't need to consider the suitability of the investment recommendation. This is because Mrs Y should have been advised to remain in the DB scheme and so the investments wouldn't have arisen if suitable advice had been given.

Summary

I don't doubt that the flexibility, control and potential for alternative death benefits on offer through a SIPP would have sounded like attractive features to Mrs Y. But KDWFS wasn't there to just transact what Mrs Y might have thought she wanted. The adviser's role was to really understand what Mrs Y needed and recommend what was in her best interests.

Ultimately, I don't think the advice given to Mrs Y was suitable. She was giving up a guaranteed, risk-free and increasing income. By transferring, Mrs Y was very likely to obtain lower retirement benefits and, in my view, for the reasons I've explained, there were no other particular reasons which would justify a transfer and outweigh this. Mrs Y shouldn't have been advised to transfer out of the scheme just to repay debts that were affordable, and the alternative death benefits weren't worth giving up the guarantees associated with her DB scheme.

So, I think KDWFS should've advised Mrs Y to remain in her DB scheme.

Of course, I have to consider whether Mrs Y would've gone ahead anyway, against KDWFS's advice. I've considered this carefully, having regard for the concerns KDWFS says Mrs Y had about the size of her mortgage. But I'm not persuaded that Mrs Y would've insisted on transferring out of the DB scheme, against KDWFS's advice. Again, Mrs Y was an inexperienced investor with a cautious attitude to risk and this pension accounted for the majority of her retirement provisions.

I'm not persuaded that Mrs Y's preference for reducing her mortgage and indebtedness, or the appeal of alternative death benefits, meant that she would've insisted on the transfer knowing that a professional adviser, whose expertise she had sought out, didn't think it was suitable for her or in her best interests. If KDWFS had explained that Mrs Y could retain her guaranteed pension – which she was unlikely to improve upon - and still meet her objectives, albeit in a different timescale than she might've initially preferred, I think that would've carried significant weight. And so, if KDWFS had provided Mrs Y with clear advice against transferring out of the DB scheme, explaining why it wasn't in her best interests, I think she would've accepted that advice.

In light of the above, I think KDWFS should compensate Mrs Y for the unsuitable advice, using the regulator's defined benefits pension transfer redress methodology.

Putting things right

A fair and reasonable outcome would be for the business to put Mrs Y, as far as possible, into the position she would now be in but for the unsuitable advice. I consider Mrs Y would have most likely remained in the occupational pension scheme if suitable advice had been given.

KDWFS 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>.

For clarity, I understand Mrs Y has not yet retired. So, compensation should be based on the scheme's normal retirement age of 60, 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 PS22/13 and 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 Mrs Y's acceptance of the decision.

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

- calculate and offer Mrs Y redress as a cash lump sum payment,
- explain to Mrs Y before starting the redress calculation that:
 - her 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 her DC pension
- offer to calculate how much of any redress Mrs Y receives could be augmented rather than receiving it all as a cash lump sum,
- if Mrs Y accepts KDWFS's offer to calculate how much of her redress could be augmented, request the necessary information and not charge Mrs Y for the calculation, even if she ultimately decides not to have any of her redress augmented,

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

Redress paid to Mrs Y as a cash lump sum includes compensation in respect of benefits that would otherwise have provided a taxable income. So, in line with DISP App 4, KDWFS 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 Mrs Y'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 £170,000, 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 £170,000, I may recommend that the business pays the balance.

My final decision

Determination and money award: I uphold this complaint and require KD Wright Financial Services Limited to pay Mrs Y the compensation amount as set out in the steps above, up to a maximum of £170,000.

Recommendation: If the compensation amount exceeds £170,000, I also recommend that KD Wright Financial Services Limited pays Mrs Y the balance.

If Mrs Y accepts this decision, the money award becomes binding on KD Wright Financial Services Limited.

My recommendation would not be binding. Further, it's unlikely that Mrs Y can accept my decision and go to court to ask for the balance. Mrs Y may want to consider getting independent legal advice before deciding whether to accept any final decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs Y to accept or reject my decision before 23 June 2023.

Ben Stoker
Ombudsman