DRN-4124136

The complaint

Mrs A complains about the advice True Potential Wealth Management LLP gave to her 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 A spoke with True Potential in December 2016 to discuss her previous pension and retirement needs. At that time, within the previous year, she'd been made redundant from her employer of around 20 years and had found work with another firm. She'd been a member of her former employer's DB scheme until redundancy.

True Potential completed a fact-find to gather information about Mrs A's circumstances and objectives. Amongst other things it noted that:

- Mrs A had not yet turned 48 years old. She was in good health, divorced with two children aged around 11 and 13. She received child and spousal maintenance of £30,000 per year.
- Mrs A was employed earning around £110,000 before any bonus (of up to 25% of salary) which might be payable.
- She and her employer were together paying around £916 a month into her current employer's defined contribution ('DC') pension scheme.
- Her home was worth around £1.6 million with an outstanding mortgage of around £410,000, which she was repaying at around £2,055 a month.
- She was considering selling her home and downsizing once her youngest daughter had finished university, probably when Mrs A was 58 years old.
- She had £130,000 invested in savings and £15,000 held in shares.
- She had further savings of £50,000 intended as an emergency fund.
- She wanted to retire at "55-60" while maximising her tax free cash ('TFC').
- She believed she would require an income of around £3,500 a month net once her mortgage was repaid.

True Potential carried out an assessment of Mrs A's attitude to risk, which it deemed to be balanced. It gathered information about Mrs A's DB scheme and obtained a transfer value analysis (TVAS) report. Mrs A's DB scheme had a cash equivalent transfer value ('CETV') of around £1,030,100. If Mrs A took her DB benefits at age 55 the Scheme would pay her TFC of £194,958 and a yearly income of £29,243 (gross). If she didn't take TFC then the yearly pension would be £41,505. The growth rates required (the critical yield) to match those benefits from an alternative arrangement would be 7.8% and 10.94% respectively. If she remained in her scheme until its normal retirement age of 60 it would pay her TFC of £207,234 and an income of £36,473. If she didn't take TFC her yearly income would be £52,538. The critical yields to match those benefits were 4.45% and 6.64%.

In January 2017 True Potential sent Mrs A its suitability report setting out its analysis and recommendations. It recommended that she should transfer the funds from her DB scheme to a named SIPP. True Potential said that by transferring Mrs A would be able to achieve her objectives of:

- Having sufficient levels of income in retirement.
- Have the flexibility to vary her income in retirement.
- Provide death benefits for her daughters.

Mrs A accepted True Potential's advice and transferred her DB funds into the named SIPP. In December 2021 Mrs A complained to True Potential that its 2017 advice wasn't in her best interests. Amongst other things she said True Potential had made a "huge play" about her DB pension being lost if she died. True Potential replied in 2022. In short it said its suitability report had highlighted that providing capital benefits on her death could result in lower income in retirement. It had noted in its fact-find that, with property equity and death in service cover, Mrs A's daughters were already financially secure should Mrs A die. As such its transfer recommendation was not made because of the availability of death benefits.

True Potential added that if Mrs A had taken income from her DB scheme at age 55 that would have left her with a shortfall in the early years of retirement. So it was likely that she would always have had to transfer her DB funds. But it added that after her state pension became payable, at 67, she would have had excess taxable income.

True Potential also said that its "computer analysis", based on 5% investment growth a year, minus charges, showed that her pension fund would be worth around £1.44 million by the time she was 55 and by taking that as drawdown would last her beyond her life expectancy. It said its recommendation had allowed Mrs A to meet her retirement goals.

Mrs A brought her complaint to us. One of our Investigators looked into it. He recommended it should be upheld and said True Potential should calculate if Mrs A was owed compensation. In summary he said that, given her income needs, Mrs A was always likely to have a shortfall from her DB scheme whether she took funds at 55 or 60. But he said she could make up this shortfall from other sources including her savings and investments. He noted Mrs A had said that she was prepared to compromise on her income needs but True Potential hadn't examined this in detail. He added the critical yields to match the benefits from the DB scheme were unlikely to be met. And as such Mrs A was likely to receive benefits of a lower value than her DB scheme in retirement by transferring.

Our Investigator added that if Mrs A wanted to leave a legacy for her daughters she could have considered insurance. So he didn't think the recommendation to transfer was in Mrs A's best interests.

True Potential didn't initially reply to our Investigator's assessment of the complaint so he referred it for an ombudsman's consideration. True Potential has since provided some further comments. Amongst other things it said that given the size of Mrs A's CETV life assurance wasn't affordable. Also, as Mrs A's DB fund was insufficient to meet her needs and given her circumstances and objectives, its recommendation was suitable for her. It also questioned the applicable retirement date.

As True Potential didn't accept our Investigator's assessment of the complaint it's been passed to me to determine.

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 bringing this complaint and in replying to it Mrs A and True Potential have made a number of comments. I've considered everything on file. But, in this decision I don’t intend to address each and every issue raised. Instead I will focus on what I see as being the outstanding matters at the heart of Mrs A’s complaint and the reasons for my decision.

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 Businesses (‘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

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

Financial viability

True Potential carried out a transfer value analysis report (as the regulator required) showing how much Mrs A’s pension fund would need to grow by each year in order to provide the same benefits as her DB scheme (the critical yield).

True Potential gave its advice during the period when this Service was publishing 'discount rates' on our website for use in loss assessments where a complaint about a past pension transfer was being upheld. I’ll explain that a discount rate is a measure of what an investment is likely to grow at in the future. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, we find it a useful tool to establish whether an investment is likely to match, or exceed, the required growth rates to make a DB transfer financially viable when the advice was given.

Mrs A hadn't yet reached age 48 at the time of the advice and her preference was to retire at age 55, although her scheme's normal retirement age was 60. The scheme did allow early retirement, although the benefits payable would be reduced. The critical yield required to match Mrs A's benefits at age 55 was 10.94% if she took a full pension and 7.8% if she took TFC and a reduced pension. The critical yields reduced to 6.64% for a full pension and 4.45% if she took TFC and a full pension at age 60. The relevant discount rate for Mrs A's retirement at age 55 was 3.4% for 7 full years to retirement. This rose to 4% at age 60 for 12 full years to retirement.

I've kept in mind that the regulator's projection rates had 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 A's balanced attitude to risk and also the term to retirement. There would be little point in Mrs A 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 lowest critical yield was 4.45% at age 60 and all the discount rates were below that I think Mrs A was likely to receive benefits of a lower overall value than the DB scheme at retirement, as a result of investing in line with that attitude to risk.

True Potential said a comparison between critical yields and discount rates wasn't appropriate as the DB scheme would also leave Mrs A with a shortfall in retirement. I've dealt with Mrs A's income needs below. However, I've addressed here True Potential's comment in the light of the question of financial viability. Under COBS 19.1.2 the regulator required firms like True Potential to compare the benefits likely to be paid under a DB scheme with those payable under a personal pension by using reasonable assumptions. And while True Potential wasn't required to use discount rates to make that comparison I'm satisfied it remains a reasonable yardstick for that purpose.

Similarly, when it produced its suitability report True Potential said that a critical yield of 7.8% for Mrs A's desired retirement at age 55, while taking TFC, wasn't achievable. But it said that critical yield figures were based on the costs of buying an annuity on the same basis as the benefits provided by the DB scheme. And, as Mrs A didn't want an annuity, it implied the critical yield wasn't an appropriate measurement tool. But the regulator required True Potential to consider the rate of investment growth that would have to be achieved to replicate the benefits being given up. So, at that time, it needed to provide an analysis based on the critical yield. And I do think it is a relevant consideration here, particularly as I don't think Mrs A could realistically say with any certainty whether she would want to take a regular income at retirement or not. She wasn't expecting to retire for at least another seven years. It's entirely possible that Mrs A would want at least some guaranteed income in retirement (which she could achieve by taking benefits from the DB scheme).

True Potential's said its computer analysis shows that Mrs A would have been able to meet her income needs by drawdown from a SIPP for the rest of her life. But True Potential's paperwork doesn't show all the inputs or the assumptions its used. It has said its analysis was based on a consistent investment return of 5%. This is not an impossible return for an investor with Mrs A's attitude to risk, and it does accord with the regulator's mid-level projection rate. But given the volatilities in the investment markets I think consistent growth at that level might well be difficult to achieve.

Further, it appears that its analysis was not "stress tested" to allow for things like market crashes. And a fall or reduction in the sum invested at an early stage can have a far greater impact on the investment returns over a longer term. That's because there is a smaller sum remaining to grow. So the computer analysis doesn't appear to show what would happen if the SIPP grew at lower levels, or that it allowed for any periods of poor investment performance. So I don't think they paint a complete picture of the likely future scenarios that Mrs A could be facing

Additionally, it would seem that True Potential has assumed that Mrs A would leave her funds invested, with exposure to the same elements of investment risk, after she'd retired and begun taking an income from her fund. But that assumption doesn't allow for an element of 'de risking'. I'll explain that its common, as investors get nearer to retirement, for the risk to be spread and some funds to be transferred to lower risk investments or bonds to attempt to protect those sums from the volatilities of the investment markets. But, there's no evidence True Potential's analysis considered that. And instead it relied on consistent mid-level growth for the rest of Mrs A's life. It follows that I'm not persuaded that True Potential's computer analysis is a compelling reason to disregard the comparison between critical yield and discount rates. And that comparison shows that Mrs A is likely to be worse off as a result of transferring.

For this reason alone I don't think a transfer out of the DB scheme was in Mrs A's best interests. Of course financial viability isn't the only consideration when giving transfer advice. There might be other considerations which mean a transfer is in a consumers best interests. I've considered this below. When doing so I've been mindful that True Potential's role was to find out what Mrs A's wants and needs were and why. Its role wasn't simply to do what she wanted without appropriate analysis and challenge of her motives for doing so.

Flexibility, early retirement and income needs

It's evident that when discussing her goals Mrs A preferred to retire early. True Potential's fact-find originally records that was at 55 – 60. So it seems that, initially at least, her goal was to retire at some undecided point before she reached 60. But by the time True Potential gave its advice Mrs A's preference was to retire at 55.

I can fully understand Mrs A's wish to retire early. I think most people would say that they would like to retire early if given the chance. I also think most people would understand that having the opportunity to retire early isn't worth compromising their income security for the remainder of their retirement for. It seems to me that this is something Mrs A was likely to reassess once she approached age 55. In fact Mrs A will turn 55 next year but she's indicated that she has no concrete plans to retire at present. And as such, I think early retirement was something that was – most likely – nice to have rather than a genuine need for her.

For most people, early retirement means a significant drop in income. And that would negatively impact most individuals' spending power and lifestyle choices. So, when faced with that prospect at an early retirement age, most people choose not to retire. Instead they opt to continue working to support their current and future lifestyle options. And that seems to be a more likely prospect for Mrs A. But there's no evidence that True Potential seriously challenged her wish of early retirement at age 55. So I don't think it met its obligations to challenge her objectives in light of what she would be giving up.

Mrs A was still over seven years away from 55 and 12 from 60. So she had no need to make an urgent decision to transfer out of her DB scheme when she did. And, if she still felt she wanted to retire before age 60 and thought the income from her DB scheme wasn't enough for her needs at that time, she could have considered transferring her DB benefits to an alternative arrangement at that point. But that wasn't a decision she needed to make when she was still only 47 years old. However, it doesn't appear True Potential put that option to her.

True Potential had calculated in its fact find that Mrs A would need an income in the region of £42,000 a year net in retirement. But, in its suitability report it said she would need between £3,000 and £4,000 a month net, roughly equivalent – at that time – to between £42,000 and £61,000 gross per year. And True Potential recorded that Mrs A wanted to take TFC, although it didn't say what she intended to use those funds for. However, her DB scheme would have paid her £41,505 at age 55, just short of her lower income level of £42,000 (gross). But that wouldn't have given her access to TFC. If she wanted to take TFC as well at age 55 the DB scheme would have paid her a gross yearly pension of £29,243 together with TFC of £194,958. But, if she'd insisted on retiring at 55 that wouldn't have been her only source of income.

It's not clear from True Potential's file how long Mrs A could expect to receive child or spousal maintenance for. But it's possible it would have stopped by the time she reached 55. However, she had other income sources. Aside from her emergency fund of £50,000, she had savings and shares amounting to around £145,000, which she could have drawn down income from if she'd needed to. Also she had her new employer's DC pension, which was increasing by around £916 a month. So, assuming she maintained those contributions to that, without factoring in any allowance for investment growth, that could be worth around £77,000 by her preferred retirement age of 55. And she could have used these sources of income to top up her DB scheme pension if she'd remained in the scheme.

Further, it's worth pointing out that, retirement at age 55 wasn't Mrs A's only option. She'd told True Potential that, at some point in the future she wanted to downsize her property and buy a smaller one. Although she anticipated this wouldn't be until her youngest child was scheduled to finish university, which should have been when Mrs A turned 58. So, at that point she could have downsized and used any equity to both fund the purchase of her new home and also to provide an additional income.

It's also notable that, at age 58, the actuarial reduction for Mrs A taking early retirement from her DB scheme would have meant a smaller reduction in her annual pension. From what's on file I can see that, at age 58 she would have been entitled to a full pension of around £47,500. I don't have the figures for TFC and a reduced pension at that time, but those are likely to have been in the region of £200,000 with a pension of around £34,000. And again, by that time it's likely her DC pension and savings could have increased. So this might have been a better consideration for her. And, again, if she didn't consider she had enough income from her DB scheme at that time then she could have looked into transferring at that point. But, there's no evidence that True Potential discussed with her that deferring her preferred retirement age and decision to transfer, might be in her best interests, as I think it should have done

Also, had she remained in work until 60 then her DB fund alone would have come far closer to meeting her income needs without the need to consider income from other sources. And, by that time, her DC pension could have been worth in the region of £130,000, which could have helped her to make up any income shortfall.

So it's likely Mrs A could have met her income needs without giving up the safeguarded benefits from her DB scheme. So I don't agree with True Potential that Mrs A was always likely to have transferred out of the DB scheme.

Further, it's not the case that Mrs A wouldn't have had any flexible access to funds without transferring. That's because she would have been able to draw down sums from her DC pension and savings. So while the option of drawing all her pension income flexibly might seem like something that would be nice to have, I can't see that Mrs A had any genuine need for that flexibility that would be worth giving up guaranteed benefits for at the time that True Potential gave its advice. So I don’t think it was in her best interests to transfer.

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. And I note that the suitability report says that a key objective for Mrs A was allowing her daughters to inherit her pension on her death. So the lump sum death benefits on offer through a SIPP were likely an attractive feature to Mrs A. That’s because whatever was left within Mrs A’s SIPP at the date of her death would be passed on to her daughters. But whilst I appreciate death benefits are important to consumers, and Mrs A might have thought it was a good idea to transfer her DB scheme to a SIPP because of this, the priority here was to advise Mrs A about what was best for her retirement provisions.

A pension is primarily designed to provide income in retirement – not a lump sum to family after death. But in transferring out of her DB scheme Mrs A was essentially giving up a guaranteed, index linked, increasing income in retirement, for the potential for a lump sum for her daughters that they may not need for many years to come. And by that time, the fund could have been depleted by Mrs A’s withdrawals from it.

It’s also worthwhile pointing out that True Potential’s fact-find referred to Mrs A having death in service cover, presumably from her employer, although the level of cover isn't given. But as her only dependents at the time, it’s likely that if she had died before retiring, that would have provided her daughters with a significant financial cushion.

Also, Mrs A had equity in her property and savings which she could pass to her daughters in the event of her death. In fact True Potential said it recorded in its fact-find that Mrs A’s daughters were “very financially secure”. But it hasn't pointed that out to Mrs A at any point in its suitability report. Instead it said that by transferring Mrs A could ensure she could pass on her pension benefits to her daughters. So there’s little evidence that it sought to challenge Mrs A’s objectives for transferring while pointing out that her daughters were unlikely to *need* the additional funds on her death.

If Mrs A genuinely wanted to leave an additional legacy for her daughters, which didn’t depend on investment returns or how much of her pension fund remained on her death, then life or term insurance might have been a better solution for her. True Potential said that – given the size of her CETV – life cover would have been prohibitively expensive. However, the amount of Mrs A’s CETV is irrelevant. True Potential assumed that Mrs A would have wanted a policy which matched the full value of her CETV. But her daughters would only ever have been likely to receive that sum if she died before reaching pension age or otherwise very soon after it. And there was nothing to indicate that was a likely prospect. Otherwise the sums available for a legacy for Mrs A’s daughter would reduce as she drew down money from her SIPP, so the full CETV was unlikely to be available as a legacy for her daughters. Instead a more reasonable solution would have been to ask Mrs A how much extra she wanted to leave to her daughters and then establish if she could find an affordable policy based upon that sum. But I can't see that True Potential raised this with her.

Overall, I don’t think different death benefits available through a transfer to a SIPP justified the likely decrease of retirement benefits for Mrs A. And I don’t think that insurance was properly explored as an alternative.

Summary

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

Ultimately, I don't think the advice True Potential gave to Mrs A was suitable. She was giving up a guaranteed, risk-free and increasing income. By transferring, Mrs A was likely to obtain lower retirement benefits and in my view, there were no other particular reasons which would justify a transfer and outweigh this.

So, I think True Potential should have advised Mrs A to remain in her DB scheme.

Of course, I have to consider whether Mrs A would've gone ahead anyway, against True Potential's advice. I've considered this carefully, but I'm not persuaded that Mrs A would have insisted on transferring out of the DB scheme, against True Potential's advice. I say this because Mrs A was not an experienced investor. She had a balanced attitude to risk and this pension accounted for the majority of her retirement provision. So, if True Potential had provided her with clear advice against transferring out of the DB scheme, explaining why it wasn't in her best interests, I think she would have accepted that advice.

In light of the above, I think True Potential should compensate Mrs A 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 True Potential to put Mrs A, as far as possible, into the position she would now be in but for the unsuitable advice. I consider Mrs A would have most likely remained in the occupational pension scheme if suitable advice had been given.

True Potential must therefore undertake a redress calculation in line with the rules for calculating redress for non-compliant pension transfer advice, as detailed in the regulator's 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, Mrs A has not yet retired, and she has no plans to do so at present. So, compensation should be based on the scheme's normal retirement age of 60 (and not 65 as our Investigator mistakenly said), 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 A'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, True Potential should:

- calculate and offer Mrs A redress as a cash lump sum payment,
- explain to Mrs A 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 her redress prudently is to use it to augment her DC pension
- offer to calculate how much of any redress Mrs A receives could be augmented rather than receiving it all as a cash lump sum,
- if Mrs A accepts True Potential's offer to calculate how much of her redress could be augmented, request the necessary information and not charge Mrs A 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 A's end of year tax position.

Redress paid to Mrs A 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, True Potential may make a notional deduction to cash lump sum payments to take account of tax that Mrs A would otherwise pay on income from her pension. Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to Mrs A'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

<u>Determination and money award</u>: I uphold this complaint and require True Potential Wealth Management LLP to pay Mrs A the compensation amount as set out in the steps above, up to a maximum of £170,000.

<u>Recommendation:</u> If the compensation amount exceeds £170,000, I also recommend that True Potential Wealth Management LLP pays Mrs A the balance.

If Mrs A accepts this decision, the money award becomes binding on True Potential Wealth Management LLP. My recommendation would not be binding. Further, it's unlikely that Mrs A can accept my decision and go to court to ask for the balance. Mrs A 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 Ms A to accept or reject my decision before 17 August 2023.

Joe Scott
Ombudsman