DRN-4158426

The complaint

Through his representative, Mr S has complained that IWC Financial Ltd unsuitably advised him to transfer his employer's defined benefit (DB) pension to a personal pension in 2019.

What happened

Mr S was speaking to his usual financial adviser at the end of 2018 about a potential transfer from his DB scheme. That adviser obtained details of a cash equivalent transfer value (CETV) from the scheme on 3 January 2019, but didn't hold the required permissions to provide DB transfer advice. So, they referred Mr S to IWC.

Mr S was being offered a CETV of £164,736.25 as an alternative to a scheme pension projected to be £6,242pa from age 65 plus a tax-free cash sum of £42,830. The same figures at age 60 were projected to be £3,664pa plus £24,427. He'd built up 14.5 years' service in the scheme.

Mr S first met with an adviser from IWC on 7 January 2019, and further meetings took place on 2 & 26 February and 21 March. His usual financial adviser attended the meeting when advice was given.

IWC completed a fact find to establish Mr S' circumstances and financial objectives. He was aged 51 at the time and divorced, but with four children ranging from age 14 to 29. He was in good health and had been self-employed for 10 years, earning about £12,000pa. This was unlikely to change. All income was being used up by regular and discretionary spending.

He had a 'lowest medium' (4 out of 10) attitude to risk, assessed from a questionnaire which included saying that he had been 'extremely cautious' in the past; was put off from investing by experiencing substantial losses; was more concerned about suffering losses than making gains; would rather know his returns were guaranteed; and would rather invest in a bank account than shares.

The printout from this questionnaire noted that some of Mr S's answers were inconsistent, but that Mr S realised *"you must take some risk to achieve reasonable returns over the longer period hence a fully guaranteed return is not actually what you required, but a more stable rate of return".*

Mr S's assets and liabilities were as follows:

- personal pensions with Aviva worth £18,100 to which he wasn't contributing.
- £15,000 of savings in a deposit account.
- A £38,000 interest-only mortgage due for repayment at the time of the fact-find, and an endowment expected to pay out £28,500.
- So, he was borrowing £15,000 on a repayment basis to be cleared at about age 58.
- He was expecting a £60,000 inheritance from the sale of his elderly mother's home plus some of her savings.

The adviser wrote *"death benefit"* under the 'soft facts' section of the fact find. Consequently, he obtained quotes for whole of live cover for a benefit amount that compared with the DB transfer value. The monthly premium was £248 guaranteed, or £149 reviewable.

He noted that Mr S had no concerns about the solvency of his former employer. Mr S had selected that the DB scheme was a major part of his pension provision which *"should be protected as far as is reasonably possible",* and he didn't consider it would be appropriate to expose these benefits to anything other than a minimal level of risk. But he would prefer to take control of his pension as he didn't require the guaranteed inflationary increases and preferred the ability to pay death benefits to children irrespective of their age – and access lump sums without being required to take an income.

IWC issued a suitability report dated 19 March 2019. Within the report IWC recommended Mr S transfer the DB scheme to a Prudential personal pension and to invest in the Prufund Cautious Fund. This offered a smoothed investment return with an expected growth rate of 5.5%pa before any charges. IWC noted Mr S had the following objectives, which formed the basis of its reasons for recommending the transfer:

- Take a £10-20,000 tax free lump sum at age 55 to help pay for his daughter's wedding. (Noted as 'potential wedding' on the fact find)
- Take a further £20,000 lump sum at age 56 to purchase a campervan
- Potentially, access other funds on an *ad hoc* basis to help his other children.
- Defer taking further income from the pension until he retired at age 60, when he desired £1,000 per month net (i.e. similar to his current earnings)
- Reduce the income drawn once he received his state pension (£8,575pa) at age 67
- For all his children to benefit from his pension savings should he pass away, even those not classed as dependent on him

The analysis IWC carried out included explaining:

- Assuming that he took tax-free cash at the scheme's normal retirement age of 65, he'd need his transferred fund to grow at a critical yield of 6.47% pa to match the DB scheme pension (or omitting the spouse's pension and increases, 2.55%).
- The same figure to age 60 was 4.66% pa (or -2.1%pa omitting the spouse's pension and increases).
- Assuming that he took tax-free cash at the scheme's normal retirement age of 65, the estimated fund required now to provide the same benefits as the DB scheme was £301,298 (or omitting the spouse's pension and increases, £179,030).
- The same figure for taking benefits at age 60 was £204,964 (or omitting the spouse's pension and increases, £113,653).
- If Mr S took drawdown of the same tax-free cash and increasing income benefits that the DB scheme would provide and it grew at the medium projection rate (but after charges), the fund could last from age 65 to 100, or from age 60 to 120+.

IWC went on to say:

> *"If your sole purpose in transferring out was to match the guaranteed index linked income, including spousal income, then my advice would be to stay in the scheme. In my professional opinion if you were transferring to buy an annuity that matched the schemes benefits at 60 or 65, I could not guarantee the relevant critical yield would be achieved year on year, thus putting you potentially in a negative income position.*
>
> *However, you have no intention on buying an annuity for the reasons detailed earlier in the report as this style of contract does not meet your retirement aims and objectives. Also, the flexibility, death benefits, ongoing lump sums etc are much more important to you than a fixed, guaranteed*

inflation linked income, I am happy to provide a positive recommendation to transfer to a more flexible personal pension arrangement."

IWC calculated that Mr S had scope to access £12,000pa from a drawdown fund between ages 60 and 67, then reducing this down to account for the state pension. It said that the cashflow analysis remained positive over the rest of his lifetime compared with the DB scheme, and would still do if he experienced negative returns in the first three years.

The printout provided appears to be based on a set of example investment returns (some positive, some negative) in each year up to age 100. This suggested Mr S could meet his income objective from the transferred fund and other assets and state pension combined up to approximately that age, allowing for the planned lump sum expenditure above.

I note that the sale was referred for further checking on account of Mr S transferring at under age 55, having other assets of less than £50,000 and other liabilities – but was passed under IWC's compliance process because a transfer was the only way of achieving Mr S's objectives.

Mr S accepted IWC's recommendation, and the transfer took place on 2 May 2019 for the amount originally quoted. The fees for the transfer were 4% initially and 0.5%pa for ongoing reviews. This was in addition to the charges for the pension of about 1.1%pa.

Mr S complained to IWC through his representatives in February 2022 that the advice was unsuitable because he was highly unlikely to match the benefits in the DB scheme, and there were no exceptional circumstances that justified transferring. IWC disagreed with the complaint, saying that a transfer of the pension was the only and best option to achieve Mr S's retirement objectives.

One of our investigators considered the complaint. On 6 April 2023, she said, in summary:

- The large gap between the CETV and TVC amount, and the critical yields quoted, all showed that Mr S wasn't going to be able to replicate the scheme benefits in a guaranteed way by purchasing an annuity outside the scheme. (The figures the investigator referred to here were higher ones assuming no tax-free cash was taken.)
- One reason for this was because the regulator's lower projection rate of 2% and medium rate of 5% - representing returns a little above and below Mr S's claimed low to medium attitude to risk – didn't compare favourably with these yields.
- Moreover, Mr S had little capacity to take loss with his primary source of pension provision other than state benefits.
- IWC was able to demonstrate that Mr S's cashflow objectives would be met by the transfer from combining the drawdown with his other sources of income. But it carried with it the risk that Mr S would over-deplete his pension pot, because there were non-specified payments that he would also like to make to his three other children.
- Even though it factored in poorly-performing years, she didn't consider the forecast returns IWC projected for Mr S's portfolio were robust enough to cover all potential scenarios for investment performance – given in particular his low capacity for loss.
- Alongside his state pension, the DB scheme went a long way to meeting his income need from guaranteed sources at virtually no risk.
- Mr S didn't yet have a genuine need to access sums through a flexible pension at the time, as that could have been revisited closer to age 55. He may have built up further savings over that period and reduced the draw on accessing his pension, or been able to manage just by accessing his smaller Aviva pension.
- Likewise, the intended strategy of taking more income from drawdown from age 60 to

67 than afterwards, could easily have altered by the time Mr S reached that age.

- Most people would like to retire early if given the option, but IWC didn't consider carefully enough if Mr S could actually afford to do so – particularly given his intention to assist his other three children financially.
- There might also not have been a large pension fund remaining on Mr S's passing, as a result of investment performance and this planned expenditure. So the adviser should have cautioned Mr S against transferring because of the death benefits.
- The DB scheme would potentially provide benefits for his two youngest children, while they were still dependent. But this could have been augmented by taking out term assurance (rather than whole of life assurance) at relatively low cost.
- Financial planning wasn't simply about wish fulfilment and facilitating whatever course of action Mr S wanted to take. He was financially inexperienced given his lack of other investments and the small private pension he had. It was incumbent upon the adviser to give suitable advice, and his need for a secure lifetime income was best met by remaining in the DB scheme.

IWC told the investigator that it didn't accept her findings but was taking a pragmatic approach, so it would carry out a loss assessment calculation. Mr S's representative asked for this to be based on Mr S retiring at the scheme's normal retirement age of 65, as he in fact had no plans to retire from work until age 67. The investigator shared this request with IWC and it agreed on 21 April that when it conducts the calculation it would use the scheme's normal retirement age of 65.

The investigator asked IWC on 28 April to clarify its intentions in carrying out the calculation, and whether that meant it accepted that Mr S should receive any redress due. IWC replied that it was agreeing to carry out calculations, but only went as far as saying it would then share the results of those with this service. Mr S's representative didn't regard this as an admission of liability and wanted the complaint to remain open until the loss calculation had been carried out.

The queue for cases awaiting an ombudsman's decision is relatively short at present and we cannot, unfortunately, keep cases open indefinitely. The investigator notified both parties on 12 May that the case would be put into this queue.

I understand that Prudential notified Mr S's representative on 17 May that it would provide the information needed for the calculation within 10 working days, and that this was relayed to IWC. This was revised to two working days from 9 June. This service hasn't been updated further, but I understand that these calculations can take some time.

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'm satisfied that IWC has been given a full opportunity to respond to the investigator's view, issued some 12 weeks ago. It has said it doesn't accept the view, but without giving reasons – and we notified it some 7 weeks ago that the complaint would be passed to an ombudsman and allowed it a further opportunity to make further representations. Naturally it is IWC's choice to embark upon calculations. However, the case has now reached me in the decision queue without agreement between the parties that it has been settled. And it is the methodology that should be used to calculate loss, rather than the result, that this service can determine.

I've reviewed all of the evidence and submissions and agree with the investigator's view, for much the same reasons. Although she referred in her view on the critical yields and TVC for a pension without tax-free cash being taken, I've put all of the other figures we have in the background above.

At first sight the figures to age 60 look more achievable than those to age 65. However I don't have confidence in the figures to age 60 because the stated assumption at the end of the analysis printout is that the quoted early retirement factor has simply been applied to the DB pension revalued to that age. The scheme's letter to IWC quite clearly states it should be applied to the projected pension revalued to age 65, assuming 2.5%pa inflation first. The effect of this is that the critical yields and TVC sums for retirement at age 60 should not have been as low as stated.

I also note that IWC ran the calculations with Mr S's marital status as unknown. If it had entered that he was divorced (single), or made any further submissions on this point, it might have been clearer what the yield or sum required would be allowing for the annual increases but *not* the spouse's pension – which obviously wouldn't be payable in Mr S's case unless he remarried before retirement.

As it is, we only have a comparison between a figure assuming Mr S was married, and another without any spouse's benefits *or increases* at all. So, the actual yield Mr S would need to achieve to match the income *plus* valuable inflationary increases under the DB scheme would have been part-way between 2.55% and 6.47% (to age 65), and I expect correspondingly lower – but not as low as the figures quoted – to age 60.

However in any event, and like the investigator, I'm not satisfied Mr S could realistically afford to retire fully at age 60. The income he desired in retirement was the same as what he was earning. His living costs (other than the mortgage, which by then would hopefully be paid off) were using up all of that income at the time of advice. In my view that also illustrates why Mr S's pension income keeping pace with inflation should have been important to him. As the investigator mentioned, if he stopped working at 60 then the cashflow analysis suggested it was unlikely he'd be able to give any financial assistance to his other three children on an *ad hoc* basis – without risking running out of money in later retirement.

Mr S said himself on the fact find that he didn't think he could afford to retire early. His representative says that he expects to remain working until age 67 and I don't find that unreasonable – or at the least, age 65 if he'd retained a DB pension that kicked in at that age. Given that I don't think age 60 was a realistic age for Mr S to start drawing his income, I'm referring mainly to the critical yield and TVC figures to age 65 as an indication of the risk Mr S would be taking in relinquishing his DB pension.

I agree the specific reference the adviser made to death benefits on the fact find is relevant, because Mr S was most likely to die after any of his children were dependent and able to receive anything additional from the DB scheme. So, they'd only get a refund of contributions, or the remainder of any 5-year guarantee period on his pension. I can see why he would have been interested in seeing if they could be better protected. But in my view, for someone of Mr S's relatively low attitude to risk, the critical yield for a single-life pension (but including annual increases) best represents whether he could afford to take the risk of leaving the DB scheme. That's because it might allow him to invest cautiously for an income, with at least the prospect of leaving some residual funds behind for his children on his death.

Having looked at this however, I can't fairly see that the critical yield was likely low enough to warrant Mr S taking that risk. In my view the superior death benefits under drawdown would only be notably more if Mr S died before his time. Particularly as after he'd embarked on increased expenditure up to age 67 as assumed in the cashflow analysis, there would be correspondingly less left in the pot to pass on to his children – as they'd have benefited in his lifetime rather than on his death.

Like the investigator said, the particular benefit of having more residual funds in the earlier years of drawdown could be covered by buying a decreasing term assurance policy. I think it was misleading of IWC to illustrate the expensive cost of a whole of life policy for a level sum equal to the CETV, when it was unlikely Mr S's children would receive that sum - other than in the event of his death in the very early years of drawdown.

Whilst I'm mindful of the cashflow analysis IWC also undertook, I believe that the TVC and critical yield are the most relevant figures given Mr S's circumstances. I agree with the investigator that Mr S had a low capacity for loss and this actually lowered, realistically, what risk he could afford to take on a transfer – i.e. his attitude to *transfer* risk. Given the amount he was now earning on a self-employed basis, he had been fortunate to accumulate a substantial DB pension from a previous employment. But he evidently had little spare income to increase the size of his small Aviva pension further in future.

I also don't think the way of resolving the inconsistent answers in Mr S's attitude to risk questionnaire was to encourage him to take more risk than some of his answers suggested – with the effect of making it more likely a transfer might pay off. I think Mr S's answers overall reflect his cautiousness at transferring such a significant sum, and major part of his pension provision. I consider these should have called into question whether Mr S's risk profile really was as high as 4/10 in respect of making this particular transfer. I'm not persuaded that the returns on the Prufund Cautious fund, which whilst smoothed were not guaranteed, and subject to charges, were an adequate exchange for the virtually risk-free, index-linked pension Mr S would have enjoyed from his DB scheme.

So in summary, I don't think Mr S had the appetite for, or capacity to take the risks of drawdown with the main part of his pension provision. And despite being his lack of need for a spouse's pension, I'm not satisfied the CETV being offered by the scheme was good enough value for him to be able to replicate the secure nature of the DB pension, but still incorporate the flexibility of accessing lump sums without income. Where I think the adviser went wrong is in his statement (quoted above) that Mr S should remain in the scheme *if* he wanted a guaranteed, index-linked income, and leaving Mr S to conclude that the other advantages of drawdown were worth giving this up for. I think his advice should have unequivocally been that they were not.

I've then considered whether Mr S would have followed this advice, if given. He was making plans to access lump sums more than three years away. The wedding plans were referred to as 'possible', and I note Mr S still had other cash sums and the ability to access his other Aviva pension. I wouldn't consider the camper van to be an essential expenditure as opposed to something Mr S was interested in buying. If necessary, he could have reached a compromise between drawing his DB pension early enough to have enough cashflow to do all these things he wanted, without receiving too much unnecessary income. He could, of course, have reinvested any surplus income back into the Aviva pension. To the extent that these objectives were fixed in stone, which was debateable, it was the adviser's role to outline alternatives for achieving them.

Whatever Mr S decided to do when the time came at age 55 when he could first access his pension, I can see no reason why he needed to transfer it into drawdown more than three years before that – and in the meantime put his future security at risk. Flexibility isn't needed in advance of it actually being usable. And the FCA has been clear in its guidance to firms that they should only consider a transfer to be suitable if they can clearly demonstrate, on contemporary evidence, that it's in the client's best interests (COBS 19.1.6G). I'm not satisfied IWC has demonstrated this in Mr S's case.

I’ve had regard for Mr S’s representative’s comments that he intends to remain working until at least 65 – which IWC hasn’t responded to in the investigator’s view. I note it was already intending to carry out a loss assessment assuming the DB pension was taken at that age. Given what I’ve said about Mr S’s ability to access other cash sums or his smaller Aviva pension, I consider that to be a fair assumption.

Putting things right

A fair and reasonable outcome would be for IWC Financial Ltd to put Mr S, as far as possible, into the position he would now be in but for the unsuitable advice. I consider Mr S would have most likely remained in the DB scheme if suitable advice had been given.

IWC Financial Ltd 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 (PS)22/13 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, Mr S has not yet retired, and he has no plans to do so at present. So, compensation should be based on his normal retirement age of 65, 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 S acceptance of this decision. If the redress calculation demonstrates a loss, as explained in PS22/13 and set out in DISP App 4, IWC must:

- always calculate and offer Mr S redress as a cash lump sum payment;
- explain to Mr S 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 the redress prudently is to use it to augment his Prudential plan;
- offer to calculate how much of any redress Mr S receives could be augmented rather than receiving it all as a cash lump sum;
- if Mr S accepts IWC’s offer to calculate how much of their redress could be augmented, request the necessary information and not charge Mr S for the calculation, even if he ultimately decides not to have any of the redress augmented; and
- take a prudent approach when calculating how much redress could be augmented, given the inherent uncertainty around Mr S’s end of year tax position.

Redress paid to Mr S 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, IWC 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 S’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.

My final decision

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.

Determination and money award: I uphold the complaint. I require IWC Financial Ltd to pay Mr S 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 IWC Financial Ltd pays Mr S the balance.

If Mr S accepts my decision, the money award is binding on IWC Financial Ltd. My recommendation is not binding on IWC Financial Ltd. Further, it's unlikely that Mr S can accept my decision and go to court to ask for the balance. Mr S may want to consider getting independent legal advice before deciding whether to accept this decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 28 July 2023.

Gideon Moore
Ombudsman