DRN-4209915

Financial Ombudsman Service

The complaint

Mr P complains that The On-Line Partnership Limited (On-Line) gave him unsuitable advice to transfer deferred defined benefits in an occupational pension scheme (DBOPS) into a personal pension plan (PPP). Causing him to suffer the loss of valuable guaranteed retirement benefits.

What happened

Mr P approached an adviser for On-Line about retirement planning advice in November 2016. Mr P had been made aware that his long term employer would be closing down its factory and he would become redundant in June 2018.

At the time of providing advice On-Line completed a fact-find and established that Mr P:

- Was married with no financially dependent children
- Was aged 55, about to reach 56
- Worked full time earning around £38,000 plus part time earnings of £7,000 a year
- Was married and his wife was earning around £6,000 a year
- Had sufficient household income with a monthly surplus of £1,279 a month
- Had a mortgage balance of £26,000 and no other debts
- Had a defined contribution occupational pension scheme (DCOPS) with a fund around £78,000

Mr P had deferred rights in a DBOPS that had been closed by his employer in November 2016. The DBOPS had a normal retirement age of 65 and had quoted a cash equivalent transfer value (CETV) around £330,000 guaranteed until February 2017. And On-Line understood that in June 2018 Mr P would receive a redundancy payment worth around £110,000. Mr P had decided to take his maximum tax free redundancy allowance of £30,000 and opt for the remaining £80,000 to be made as a payment into his DCOPS.

On-Line described Mr P's objectives with his DBOPS as being:

- Improved benefits of a DC pension plan
- Taking a maximum PCLS in the near future
- Be able to take flexible income withdrawals in the near future
- Have control over how his pension is invested

On-Line provided Mr P with a written recommendation dated 4 January 2017. It recommended that Mr P transfer his DBOPS to a new personal pension that would allow him to access his pension commencement lump sum (PCLS) when he needed it. It said it would allow Mr P to have control over how his pension was invested, have flexibility about the income that he took from the pension, and provide improved death benefits.

Mr P complained, via a representative, in June 2022. The complaint alleged that the advice to transfer this pension had been unsuitable as it was not in Mr P's best interests.

On-Line looked into Mr P’s complaint. It explained its recommendation, repeating what it had said in the recommendation and reiterating that it thought it met Mr P’s objectives in 2016. It didn’t uphold Mr P’s complaint.

Mr P disagreed and his representative brought his complaint to our service. Our investigator considered the circumstances at the time and was of the view that Mr P’s complaint should be upheld. She explained why she thought the transfer was likely to give Mr P lower overall benefits. And why she didn’t think that other objectives or reasons made the transfer in Mr P’s best interests.

On-Line failed to respond within the deadline and this case was referred for an ombudsman’s decision. Subsequently On-Line responded to explain that it didn’t agree with our investigator’s view. But explained that it was prepared to do a loss calculation in order to resolve the complaint. It calculated a figure for Mr P’s overall loss in a way that was in line with our investigator’s view and made that offer to Mr P.

At the time of considering this decision On-Line’s offer has not been accepted.

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 am proceeding to issue a final decision on this case in line with the rules that govern our service, namely DISP 3.5.4R(3). This rule explains that, once a provisional assessment has been provided to both parties setting out a time limit to respond, if either party indicates disagreement with the provisional assessment I should proceed to determination. In this instance, in spite of a resolution appearing close, Mr P has only accepted the provisional assessment after adding a condition of his own. And On-Line has clearly stated that it fundamentally disagrees that the case should be upheld. Even though it has made a settlement offer.

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

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 ON-LINE'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, On-Line should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr P's best interests. And having looked at all the evidence available, I'm not satisfied it was in his best interests.

Financial viability

On-Line obtained a transfer value analysis report (as required by the regulator) showing how much Mr P's pension fund would need to grow by each year in order to provide the same benefits as his DBOPS (the critical yield).

The advice was given during the period when the Financial Ombudsman Service was publishing 'discount rates' on our website for use in loss assessments where a complaint about a past pension transfer was being upheld. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, I consider they provide a useful indication of what growth rates would have been considered reasonably achievable when the advice was given in this case.

Mr P was 55 at the time of the advice and wanted to retire at 65. The critical yield required to match Mr P's benefits at age 65 was 9.1% if he took a full pension. This compares with the discount rate of 3.7% per year for around 9 years to retirement in this case.

For further comparison, the regulator's upper projection rate at the time was 2%, the middle projection rate 5%, and the lower projection rate 8%.

I've taken this into account, along with the composition of assets in the discount rate, Mr P's attitude to risk and also the term to retirement. I think Mr P was unlikely to receive benefits of a materially lower overall value than the DBOPS at retirement, as a result of investing in line with his attitude to risk.

So, in terms of trying to maximise the value of this DBOPS for Mr P, a transfer out of the DBOPS wasn't in Mr P's best interests. Of course financial viability isn't the only consideration when giving transfer advice, as On-Line has argued in this case. There might be other considerations which mean a transfer is suitable, despite providing overall lower benefits. I've considered this below.

Flexibility and income

Mr P was in a position where he was having to face life changing circumstances. He knew that he would be losing a job in June 2018 that paid him around £38,000. And he thought it was unlikely he would be able to get similarly paid work. So he was facing a severe change in his household income. And, given that he would be over 57 years by the time that happened, it is understandable that he would be looking at options to use his pensions to make up some of that shortfall.

Mr P was in the fortunate position of have a DBOPS that would give him an income around £17,500 at age 65 after being revalued. And it could be taken early in 2018 to give an income around £9,500 a year index linked. In addition to this On-Line were advising with a clear understanding that Mr P would continue contributing to his DCOPS and it would likely have over £160,000 in it by that time.

On-Line ascertained that Mr P had a target income around £24,000. Which given the estimate they obtained for his household expenditure was perfectly reasonable. It knew that he intended to continue to work in his part time position earning £7,000 a year. And that he intended to find other work or to increase his existing part time position (estimate of up to £11,000 a year). He was also intending to use £26,000 of his tax free redundancy lump sum to pay off his mortgage. Thereby reducing his net annual expenditure by around £4,000. Overall, it was highly likely that Mr P would need to find in the region of £10,000 a year from his pensions to meet his income needs if he couldn't find work to cover that shortfall.

But Mr P was 57, so had less than eight years to fund in that way before he could access his DBOPS in full in the way it was intended. On-Line's analysis made it clear that was the most valuable way to use that particular pension. And it should only consider doing otherwise if this objective couldn't be met without it. But an existing defined contribution pension plan with a fund size around £160,000 was more than likely adequate to enable Mr P to drawdown flexibly from that for eight years without exhausting it. It would likely have meant transferring it to a PPP that would allow that type of access. But this option, as well as the option of taking a combination of that and the DBOPS benefits early appear to have been given little, if any, consideration.

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. The lump sum death benefits on offer through a personal pension was likely an attractive feature to Mr P. But whilst I appreciate death benefits are important to customers, and Mr P might have thought it was a good idea to transfer his DBOPS to a PPP because of this, the priority here was to advise Mr P about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think On-Line explored to what extent Mr P was prepared to accept a lower retirement income in exchange for higher death benefits.

I also think the existing death benefits attached to the DBOPS were underplayed. Mr P was married and so the spouse's pension provided by the DB scheme would've been useful to his spouse if Mr P predeceased her. I don't think On-Line made the value of this benefit clear enough to Mr P. This was guaranteed and it escalated – it was not dependent on investment performance, whereas the sum remaining on death in a personal pension was. On-Line should not have encouraged Mr P to prioritise the potential for higher death benefits through a PPP over his security in retirement.

Furthermore, if Mr P genuinely wanted to leave a legacy for his spouse and children, which didn't depend on investment returns or how much of his pension fund remained on his death, I think On-Line should've instead explored life insurance. Ultimately, Mr P wanted to leave whatever remained of his pension to his spouse and children, which would be a lot less than the starting fund size if he lived a long life or if investment returns were poor. So, the starting point ought to have been to ask Mr P how much he would ideally like to leave to his family, and this could've been explored on a whole of life or term assurance basis, which was likely to be a lot cheaper to provide.

Overall, I don't think different death benefits available through a transfer to a PPP justified the likely decrease of retirement benefits for Mr P. And I don't think that insurance was properly explored as an alternative.

Control over investments

I think Mr P's desire for control over his pension benefits was overstated. Mr P was not an experienced investor and I cannot see that he had an interest in or the knowledge to be able to manage his pension funds on their own. So, I don't think that this was a genuine objective for Mr P. His pension fund was simply placed into an investment fund with no particular control being recommended other than the need for ongoing reviews of investment performance. That would not have been required had he remained in the DBOPS.

Summary

I don't doubt that a large PCLS, flexibility and potential for higher death benefits on offer through a PPP would have sounded like attractive features to Mr P. But On-Line wasn't there to just transact what Mr P might have thought was the best option for him. The adviser's role was to really understand what Mr P needed and weigh all of Mr P's options to recommend what was in his best interests.

Ultimately, I don't think the advice given to Mr P was suitable. He was giving up a guaranteed, risk-free and increasing income that would exceed his income needs in retirement. By transferring, Mr P was very likely to obtain lower retirement benefits and in my view, there were no other particular reasons which would justify a transfer and outweigh this. Mr P shouldn't have been advised to transfer out of the DBOPS in order to make up his income shortfall in retirement when he would have a large enough DC pot to be able to do that already. And the potential for higher death benefits wasn't worth giving up the guarantees associated with his DBOPS.

So, I think On-Line should've advised Mr P to remain in his DB scheme.

Of course, I have to consider whether Mr P would've gone ahead anyway, against On-Line's advice.

I've considered this carefully, but I'm not persuaded that Mr P would've insisted on transferring out of the DB scheme, against On-Line's advice. I say this because Mr P was an inexperienced investor with a low/medium attitude to risk and this pension accounted for a significant part of Mr P's retirement provision. So, if On-Line had provided him with clear advice against transferring out of the DBOPS, explaining why it wasn't in his best interests, I think he would've accepted that advice.

In light of the above, I think On-Line should compensate Mr P 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 On-Line to put Mr P, as far as possible, into the position he would now be in but for the unsuitable advice. I consider Mr P would have most likely remained in the occupational pension scheme if suitable advice had been given.

On-Line 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, Mr P has not yet retired, and he has no plans to do so at present. So, compensation should be based on the scheme's 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 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 Mr P'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, On-Line should:

- calculate and offer Mr P redress as a cash lump sum payment,
- explain to Mr P before starting the redress calculation that:
    - their 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 DC pension
- offer to calculate how much of any redress Mr P receives could be augmented rather than receiving it all as a cash lump sum,
- if Mr P accepts On-Line's offer to calculate how much of their redress could be augmented, request the necessary information and not charge Mr P for the calculation, even if he ultimately decides not to have any of their redress augmented, and
- take a prudent approach when calculating how much redress could be augmented, given the inherent uncertainty around Mr P's end of year tax position.

Redress paid to Mr P 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, On-Line may make a notional deduction to cash lump sum payments to take account of tax that customers 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 P'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 The On-Line Partnership Limited to pay Mr P 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 The On-Line Partnership Limited pays Mr P the balance.

If Mr P accepts this decision, the money award becomes binding on The On-Line Partnership Limited.

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

The On-Line Partnership Limited must pay the compensation within 60 days of the date on which we tell it Mr P accepts my final decision. If it pays later than this it must also pay interest on the compensation from the deadline date for settlement to the date of payment at 8% a year simple.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr P to accept or reject my decision before 8 August 2023.

Gary Lane
Ombudsman