DRN-4365549

Financial Ombudsman Service

The complaint

Mr D has complained that Inspirational Financial Management Ltd (IFM) gave him unsuitable advice to transfer his defined benefits from his occupational pension scheme (OPS) – the British Steel Pension Scheme (BSPS) – to a Personal Pension Plan (PPP).

What happened

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

In March 2016, Tata Steel UK Ltd announced that it would be examining options to restructure its business, including decoupling the BSPS from the company. The consultation with members referred to possible outcomes regarding their preserved benefits, one of which was a transfer to the Pension Protection Fund ("PPF") – the PPF is a statutory fund designed to provide compensation to members of defined benefit pension schemes when their employer becomes insolvent. The BSPS was closed to further benefit accrual from 31 March 2017.

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

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 The main defined benefit OPS had been replaced by a new defined contribution scheme.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

The scheme trustees provided Mr D with a cash equivalent transfer value (CETV) on 11 August 2017. It showed that Mr D had 27 years and 9 months' membership with a total deferred pension of £16,569 pa.

Mr D was referred to IFM by another financial adviser who didn't have the required permissions to advise on defined benefit pensions. IFM sent Mr D a questionnaire to record his personal circumstances and attitude to risk on 4 September 2017.

Mr D was 48, in good health, had a non-married partner and no children, had a retirement age of 60 (58 ideally), and was also a member of his employer's defined contribution scheme, paying in 6% of his salary with his employer also paying in another 10% and also providing four times' his salary as a death in service benefit.

Mr D indicated that the BSPS pension represented the majority of his retirement provision, and that increasing death benefits, even at the cost of his own retirement needs, was a priority. Mr D also indicated that he wanted flexibility in how his pension was paid and wanted the highest tax-free lump sum possible, and also that he was concerned about the security of his pension. It was also indicated on the questionnaire that Mr D was a low risk, conservative investor.

IFM provided its advice in a suitability report dated 13 November 2017. According to the report, the transfer value of the BSPS pension was £417,899. IFM's recommendation was to transfer the BSPS pension into a PPP with Royal London. Concerning Mr D's objectives, the report from IFM said the following:

"As a result of our discussions, it became clear that you are attracted to the flexibility of the personal pension and imagine this will suit your retirement needs better than a fixed income for life. Equally, it is very important to you that you are in control of your retirement provisions and that you can draw benefits when you want rather than being bound by scheme rules and trustee discretion. Ensuring your pension will not die with you and allowing it to be fully inherited by your family is also a key objective of yours."

IFM said that, at Mr D's preferred retirement age of 60, he could expect to receive an annual pension of £13,600 or £9,300 with a tax-free lump sum of £62,200. IFM provided a cash flow analysis assuming that Mr D drew income at the same rate as the BSPS pension from age 60 and his pension achieved a growth rate of 4% pa after fees (and inflation at 2.5%). The forecast showed that the fund would last until age 99.

IFM also calculated critical yields (the minimum annual growth rate needed) that the CETV would need to achieve to purchase a risk-free annuity with the same income as the BSPS pension as typically around 8% pa at age 65. IFM said the following:

"Our analysis has identified that the transfer values being offered fail to reflect the true value of the 'current' British Steel Scheme pension. However, the analysis has also identified that when using the drawdown alternative, relatively modest investment returns are required in order to match the pension available from the scheme and sustain it well into your old age (as shown in the chart above).

From our discussions, it is clear that you place a higher value on having choice and control over your pension fund than having a guaranteed lifetime income. Moreover, your desire to retire early may not be satisfied by the British Steel Scheme and/or the PPF and neither will they give you the flexibility you require. Equally, you are very uncomfortable about the scheme's future prospects and on balance feel the personal pension option is better for you even with the associated investment risks."

Mr D accepted the advice to transfer. But he later complained about IFM's advice after receiving a letter from the FCA explaining that he might have received unsuitable advice.

IFM didn't uphold the complaint, as it felt the advice satisfied Mr D's objectives.

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

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

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

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

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

- The critical yield to match the scheme benefits at age 65 was quoted as being around 8%. The discount rate for 16 years to retirement was 4.3% and, taking into account Mr D’s attitude to risk, along with the regulator’s low, mid and high band growth projections of 2%, 5% and 8% respectively, it was unlikely that the scheme benefits could be bettered through transferring. The critical yields were unlikely to be achievable.

- The available evidence didn’t support the position that Mr D needed flexibility in retirement, nor that he had a need to access his tax free cash and leave the remainder invested until a later date.

- Further, Mr D’s defined contribution accrual could have been used to address any flexibility requirement.

- In terms of death benefits, it was natural that Mr D would want his loved ones to be taken care of in the event of his death. But IFM hadn’t done enough to explore to what extent Mr D was willing to accept a lower retirement income in exchange for lump sum death benefits. And the size of any lump sum would in any case depend on how much remained in the pension fund in the event of Mr D’s death.

- Additionally, no dependants had been recorded as being reliant upon Mr D. He had a partner, to whom he wasn’t married, but it was possible that, at the trustees’ discretion, the spouse’s pension could have been payable to them. Mr D also had death in service benefits, along with the value of the defined contributions.

- Mr D’s desire for control over his pension funds had been overstated. He wasn’t an experienced investor and there was nothing to suggest that he wished to manage his pension funds.

- Mr D may have had concerns about the prospects for the BSPS, but these concerns should have been managed and addressed by IFM.

The investigator recommended that IFM undertake a loss calculation in accordance with regulator’s policy statement PS22/13, and as set out in the regulator’s handbook in DISP App 4 – and, given that Mr D intended to retire early, on the basis that Mr D would have opted to join the PPF. Mr D planned to retire at age 60, and so this was the age which should be used in the calculation, the investigator said.

If the redress was paid directly to Mr D, IFM could make a notional deduction for the (assumed basic rate) income tax he would have paid on the pension benefits.

Neither party submitted any further comments on the merits of the case in response to the investigator’s assessment.

But as agreement hasn’t been reached on the outcome, it’s been referred to me for review.

What I've decided – and why

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

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 IFM'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 deal with the obligations when giving a personal recommendation and assessing suitability. And the provisions in COBS 19 specifically relate to a defined benefit pension transfer.

The regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.6G that the starting assumption for a transfer from a defined benefit scheme is that it is unsuitable. So, IFM should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr D's best interests.

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 TVAS report which IFM was required to carry out by the regulator said that the critical yield - how much Mr D's pension fund would need to grow by each year in order to provide the same benefits as his defined benefit scheme – was around 8% to match the benefits he'd have been entitled to under the scheme at age 65. To match them at 60, or earlier, this would have been higher still.

- Given Mr D's recorded "conservative" attitude to risk, the discount rate of 4.3% to age 65 (which would have been lower to age 60), and the regulator's lower and middle projection rate for growth (2% and 5% pa respectively), I think Mr D was more likely than not to receive pension benefits, from either age 60 or 65, of a lower value than those he'd have been entitled to under the BSPS 2 by transferring and investing in line with that attitude to risk.

- The critical yield to match the PPF benefits at age 65 was quoted as being around 4%. I think it would be unusual for this be roughly half the critical yield required to match the BSPS benefits, but as I can't see a copy of the transfer value analysis on the file, this is difficult to verify. But even if I'm to accept this, the critical yield to match the PPF benefits at age 60 would have been higher than this. And as above, given Mr D's conservative risk rating, the discount rate to that age and the regulator's standard growth projections, I also think that it was unlikely that the PPF benefits would be matched by Mr D transferring and investing in line with his attitude to risk.

- Early retirement was clearly appealing to Mr D, as it might reasonably be appealing to a great many people, but I can't see that there was any clear analysis of the income which Mr D might actually need in retirement. And so it's difficult to determine the feasibility of Mr D retiring early through either drawdown or with the scheme benefits.

- A "retirement scenario report" prepared by IFM seemed to indicate a target income of £22,000 pa (although this rather confusingly seemed to suggest that, with a retirement date of 67, Mr D's money would run out by age 66). But if Mr D required flexibility, this would have been possible by accessing the tax free cash and benefits which would have been available from the 12 years' defined contribution accrual by age 60. Mr D could expect a scheme pension at 60 of around £13,600 pa at the date of leaving the scheme, which would be revalued in the 12 years up to age 60 – on the basis of, say, a modest 2% pa revaluation, it would therefore be around £17,000 pa from age 60. And given Mr D's income and overall contribution to the defined contribution scheme, I think it was more likely than not that any shortfall could be made up by accessing those benefits flexibly before the state pension began.

- In terms of the alternative lump sum benefits a transfer offered to his partner, the priority here was to advise Mr D about what was best for his retirement. While the CETV figure would no doubt have appeared attractive as a potential lump sum, the sum remaining on death following a transfer would likely be different if Mr D was drawing upon it, especially to a significant degree in the early years after retirement. It would also be dependent on investment performance, and so may not have provided the legacy that Mr D may have thought it would.

- My understanding is that Mr D wasn't married to his partner, and whether or not a spouse's pension would be payable to the partner in the event of Mr D's death would be at the discretion of the trustees. But there was also the five year guaranteed period of full payment after the pension had begun to be paid.

- Further, as with the investigator, I can't see that it was clearly evidenced as to why Mr D's partner would have a need for lump sum benefits. Mr D had no dependent children, and there are no details relating to the partner's own pension provision - but it seems likely that they would in any case have their own state pension. They would further likely have benefitted from any unused value remaining in Mr D's defined contribution plan in the event of his death.

- And this of course presupposes that Mr D would remain unmarried - with another 12 years until prospective retirement, Mr D's circumstances could have changed. There was no recorded prospect of Mr D marrying at the time of the advice, and so I haven't factored this specifically into the suitability assessment, but given the number of years to retirement, and the benefits to be gained by retirement age for Mr D (or rather a spouse) if indeed he did marry, I think it's worth noting that this can't necessarily be ruled out as a possibility.

- Overall, I don't think different death benefits available through a transfer justified the likely decrease of retirement benefits for Mr D. There was no identified need for a lump sum, over and above the benefits which would have been paid through either death in service benefits, the scheme provisions for death after retirement, or the fund value which would have accrued through Mr D's defined contributions.

- My view is that IFM shouldn't have encouraged Mr D to prioritise the potential for alternative death benefits through a PPP over his own security in retirement.

- I also think Mr D's desire for control over how his pension was invested was likely overstated. As with the investigator, I can't see that he had an interest in managing, or the knowledge to be able to do so, his pension funds on his own. Given his risk attitude and lack of other experience, I don't think that this was likely a genuine objective for Mr D – it was simply a consequence of transferring away from his defined benefit scheme.

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

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

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

Putting things right

I consider that it would be appropriate to use the BSPS-specific calculator here, given the BSPS-specific circumstances.

A fair and reasonable outcome would be for the business to put Mr D, as far as possible, into the position he would now be in but for the unsuitable advice.

In terms of the option Mr D would have chosen, had he been suitably advised, I've noted that there would be a 10% reduction in the starting pension entitlement within the PPF, whereas the BSPS 2 wouldn't cut the starting entitlement for deferred members.

Regarding death benefits, under the BPSP 2 the spouse's pension would be set at 50% of Mr D's pension at the date of death, and this would be calculated as if no lump sum was taken at retirement. But as Mr D was single at the time, and unless he had undisclosed plans to marry, I don't think this particular enhancement over the PPF benefits would have had much resonance for him at that time.

The reduction for early retirement under the PPF was lower and the commutation factors for the tax free cash entitlement were also slightly more favourable. And so, on the basis of prospective early retirement, both the starting income and the tax free cash would likely have been higher with the PPF.

Mr D intended to retire at 60, and indeed, as set out above, it seemed likely that he would be able to do so on the basis of his anticipated income requirement and the benefits which would be payable from all sources of pension provision.

And so this would have been a point which required careful consideration when weighing up whether he should opt for the BSPS 2 or remain in the BSPS with a likely subsequent move into the PPF. Given what I've noted above, I consider Mr D would more likely than not have remained in the occupational pension scheme and opted to join the PPF if suitable advice had been given.

Inspirational Financial Management 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 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.

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

As Mr D intends to retire at 60, compensation should be based on a calculation to that age.

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

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

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

- explain to Mr D before starting the redress calculation that:

  - its redress will be calculated on the basis that it will be invested prudently (in line with the cautious investment return assumption used in the calculation), and

  - a straightforward way to invest their redress prudently is to use it to augment their defined contribution pension

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

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

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

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

Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to Mr D's likely income tax rate in retirement – presumed to be 20%. So making a notional deduction of 15% overall from the loss adequately reflects this.

Where I uphold a complaint, I can award fair compensation of up to £190,000, 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 £190,000, I may recommend that the business pays the balance.

Determination and money award: I require Inspirational Financial Management Ltd to pay Mr D the compensation amount as set out above, up to a maximum of £190,000.

Recommendation: If the compensation amount exceeds £190,000, I would also recommend that Inspirational Financial Management Ltd pays Mr D the balance.

If Mr D accepts this final decision, the award will be binding on Inspirational Financial Management Ltd.

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

My final decision

My final decision is that I uphold the complaint and direct Inspirational Financial Management Ltd to undertake the above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr D to accept or reject my decision before 29 December 2023.

Philip Miller
Ombudsman