DRN-4435175

The complaint

Mr H complained that he was given unsuitable advice to transfer his defined benefit (DB) Occupational Pension Scheme to a type of personal pension plan, in 2018.

PSA Financial Services Limited is responsible for answering this complaint. To keep things consistent throughout this final decision, when referring to the business, I'll refer mainly to "PSA".

What happened

Mr H approached PSA in 2018 to discuss his pension and retirement needs. PSA completed a 'fact-find' to gather information about Mr H's circumstances and objectives. His circumstances at that time were as follows:

- Mr H was 54 years and 11 months old and in a civil partnership. He had no financial dependents. He was seeking financial advice about a deferred DB pension from a previous job. The cash equivalent transfer value (CETV) was around £40,635 and the normal retirement age (NRA) was 65.

- Mr H and his civil partner lived in rented accommodation and had no significant debts, assets or savings. They earned £35,000 per year and £32,000 respectively (gross) and had around £1,200 left over each month as disposable income.

- Mr H had recently suffered a heart attack around two months prior to the advice sessions although he was evidently recovering. He was taking statin type medication in the meantime.

- In addition to the pension being complained of, Mr H had a slightly larger DB pension with his current job. This isn't the subject of any complaint here.

PSA set out its advice about Mr H's smaller DB pension in a suitability report it issued on 16 May 2018. It advised him to transfer out of his deferred DB scheme. Mr H first complained to PSA about its advice in 2023. In response, PSA denied it had done anything wrong and said it had acted on Mr H's objectives at the time. He then referred his case to the Financial Ombudsman Service. One of our investigators looked into it and said the complaint should be upheld.

PSA still doesn't agree. So, as the complaint couldn't be resolved informally, it's come to me for a final decision.

What I've decided – and why

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

I've taken into account all 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'). 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 PSA'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.

I have further considered that the regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.6 that the starting assumption for a transfer from a DB scheme is that it is unsuitable. So, PSA should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr H's best interests..

I've therefore used all the information we have to consider whether transferring to a new personal pension arrangement was in Mr H's best interests.

I don't think it was, so I'm upholding Mr H's complaint.

Financial viability

PSA referred in its transfer analysis to 'critical yield' rates. The critical yield is essentially the average annual investment return that would be required on the transfer value - from the time of advice until retirement - to provide the same annuity benefits as the DB scheme. The critical yield comparison was a requirement from the regulator at the time when advising clients on DB transfers. It's also important to point out that the critical yield comparison is only one of a number of different metrics I've used to compare the different schemes. And in my view, these all point one way – that Mr H was probably going to receive lower pension benefits overall, as a result of transferring to a type of personal pension plan.

I say this because the critical yield required to match the benefits at the age of 65 in the existing scheme, was described as 13.68%. PSA said throughout its advice that Mr H may be seeking an earlier retirement due to his recent health scare, but it didn't set out any critical yields for ages younger than 65. PSA also didn't explain in its suitability report the aspects of the critical yield which were clearly showing that Mr H's pension, if he transferred, might not grow to an extent that made transferring financially viable.

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

In Mr H's case, the relevant discount rate closest to when the advice was given was only 3.8% (for a retirement at age 65). This is substantially below the critical yield figure I've set out above and so it clearly shows that exceeding the critical yield was not reasonably achievable here. I've also kept in mind that the regulator's upper growth projection rate was 8%, the middle projection rate was 5%, and the lower projection rate was 2%. Mr H was described as having an attitude to risk (ATR) which was "moderately cautious". So I think all these assumptions were showing that future growth rates of around 2 to 4% were credible expectations. Reaching the critical yield level of over 13% was almost certainly not achievable.

I've also noted that when using the NRA of 65, PSA's own transfer analysis said that in order to purchase an annuity to provide benefits of equal value to the estimated benefits provided by the existing scheme, the estimated fund required (also known as the capital value) was £132,179. Even to purchase an annuity to provide benefits of equal value to the estimated benefits provided by the existing scheme, assuming *no* spouse's pension, *no* increases in payment and *no* guarantee at retirement, the estimated fund required at 65 was still £52,929. To reiterate, these figures are found in PSA's own analysis based on data the regulator required businesses to refer to at the time. And because these figures are well above Mr H's CETV, they represent, in my view, a revealing window into the value of the guaranteed pension he could be giving up by transferring away.

I therefore think there was every reason to think that Mr H would receive lower overall pension benefits when he took retirement as a result of transferring away from the DB scheme. There would be little point in transferring if this were the case so I think this should have showed that transferring, from a financial perspective, was not right for Mr H.

But of course, these straightforward financial comparisons aren't the full story here. This is because PSA's recommendation that he should transfer out to a personal pension wasn't wholly based on the growth comparisons with his current scheme alone. Rather, PSA focussed on what it saw were the wider benefits in transferring away from the scheme. These were mainly focussed on what Mr H's apparent objectives were. I've considered these issues below.

Other reasons for transferring

I've used a combination of what was in PSA's recommendation report in May 2018 and the various client information forms it completed about Mr H, to help determine what PSA said were the main objectives for transferring out of the DB scheme:

- PSA said Mr H wanted to take approximately £10,000 tax-free cash from his pension to spend on his driveway and garden, go on holiday and build some emergency savings. He then wanted to take income of £6,000 per year until the fund was depleted.

- It said he wanted to ensure any funds left on death would be available to his civil partner.

- PSA said Mr H wanted improved performance of his pension.

PSA also refers, more generally, to three other broad areas. It says now for example that all the evidence suggested that Mr H was happy with the service he'd been provided by PSA at the time. It also implies that he had been given a significant amount of information during the advice process. PSA also added that whilst he was at the time employed full-time and working, his employment situation was "volatile" due to his recent health issue.

I will address all these topics in turn.

- *Introductory issues*

I think it's reasonable for me to start from the premise that it was PSA that was the regulated party here, not Mr H. I've noted PSA was also charging Mr H a significant fee in proportion to his relatively modest - by pension standards - CETV. The adviser's job therefore wasn't simply to transact what Mr H might have thought was a good idea. He wasn't experienced in this area and he'd gone looking for advice, was paying for it, and so probably had every expectation that the advice offered would be in his best interests.

So, I think it's irrelevant that Mr H may have initially been "happy" with the advice. What I've seen tends to show that he had no experience of these matters and probably gained a subsequent realisation that transferring away from a DB scheme might not have been right for him. As I'll set out below – I don't think it was. And to be clear, PSA clearly recommended that he should transfer away and he followed that advice.

- *Mr H's health*

I'm sure that, both for himself and his civil partner, Mr H's health and wellbeing would have been of the utmost importance. And I certainly wouldn't wish to imply that a recent heart attack wasn't of significance.

However, I think that the adviser failed to proportionately assess Mr H's overall health and what it could mean for his retirement needs. I think there was every indication at the time that Mr H may have taken his sudden illness as a prompt to evaluate his working life and his eventual retirement plans. But I don't think there was any indication that his life expectancy had become so short as to make transferring away either urgent or necessary. I say this to clarify matters as it's unclear to me what PSA is really saying about Mr H's health and its relationship to him transferring his DB pension to a personal type of plan. But in PSA's response to the complaint it said, *"at the time* [Mr H] *approached PSA for advice, he was understandably uncertain about his future given his recent disclosed health problems and concerned that he may not be able to remain in his current employment, but even more so, how long he would actually live"*.

However, I think the adviser's job here was to use their training and experience to come to the view that there was no 'hard' evidence showing Mr H was so ill that he was going to pass away anytime soon. Everything pointed to him having got through the worst of the heart attack and that he was making a recovery. So, I think saying that Mr H's life could be in danger at that time was overstating the actual prognosis. The more likely outcome of this health event was perhaps a reduction to part-time work, or potentially an early retirement from his current job at some point. I don't think the adviser properly considered these scenarios and they certainly didn't factor them in to the financial profiles.

In short, there would have been no rationale for transferring away based only on a theory that his life was in imminent danger – the prognosis generally looked much better than this.

- *Mr H's apparent objectives*

PSA supported what it had said about Mr H's health matters with other rationale. It said Mr H wanted to access his pension more or less straight away, to carry out some home improvements and that he wanted some cash for spending on a holiday and an emergency fund. However, in my view, this all needed to be considered against the original purpose of Mr H's pension and that he only had limited financial resources. The purpose of the pension was obviously to help provide a reasonable income for him in retirement rather than to use on discretionary spending. As I've said, this was his smaller DB pension but I think it was still a relevant part of his somewhat limited pension resources.

The adviser didn't go into much detail about what Mr H's retirement plans really looked like and they assumed the financial 'slack' potentially caused by him wanting to give up work completely could be taken up by using Mr H's partner's wages. So, what PSA effectively advised Mr H to do was to irreversibly transfer away from this guaranteed DB pension for life on a vague plan that wasn't yet clear. For example, the adviser didn't appear to comprehensively assess all Mr H's income needs in retirement or consider reasonable eventualities that could occur in the years ahead. Nor did they appear to consider him remaining in that scheme and retiring from that when ready to do so, even if there would be an actuarial reduction caused by him accessing the pension earlier. They just took Mr H's aspirations at face value and focussed completely on transferring away to a type of personal pension plan. They recommended that Mr H immediately access 25% of the transferred pension straightaway followed by yearly drawdowns of £6,000. However, it's not clear what the plan was after this when the drawdown amounts ran out.

Of course, I accept that Mr H wanted to enjoy some of his own money. But the spending objectives for his home and the other aspirations he had just weren't properly costed in any way and given the fee Mr H was being charged for the advice and his limited pension overall, I think these costs should have been clearly investigated and laid out. There was no explanation, for example, of why the 25% tax-free amount of over £10,000 was required for what Mr H wanted to achieve. The information at the time describes Mr H's home as being local authority provided, so I don't think substantial structural changes were on the cards here – references in the 'fact-find' mention only notional works required on the garden and / or driveway.

So, I think the adviser should have been sceptical of the requirement for such an amount for what appeared non-essential works to a council property, a holiday and other wholly discretionary spending, however nice it would have been to have been able to afford these things.

In my view, by transferring away and using the money in the way described, the adviser was recommending a pathway where Mr H's retirement income seemed much less secure. I've mentioned he had another DB pension but this was projected to pay only around £8,100 per year and a relatively small lump-sum, upon reaching the age of 65. I think it's reasonable to assume Mr H was going to try to access that pension early too at some stage and so these figures might well have become lower. So, there was a material risk here that Mr H's overall retirement income was going to be modest because he was giving up work so young. Transferring the smaller DB scheme would only exacerbate these financial uncertainties and expose Mr H to a stock market risk that showed he could be worse off. I don't think the adviser took enough account of this when advising him to leave the DB scheme.

Overall, I don't think Mr H had a genuine need to access his tax-free cash so early. He only had modest pension provisions, and I think the advice should have been for him to remain in the DB scheme and to use it – together with his other DB scheme - in exactly the way it was intended. In my view, Mr H's circumstances demanded a 'known and regular' income in the future, rather than any need for a 'flexible income' which was no more than a stock objective used to help support the transfer-away recommendation. If Mr H's circumstances changed, or if financial flexibility did become more relevant, then he could have revisited transferring this pension at a later date.

In any event, Mr H's aspirations for this non-essential spending were probably achievable through other means. We know, for instance, that at the time he and his partner had a reasonable portion of disposable income each month and even if this reduced they could still apparently meet their short-term living costs on Mr H's partner's salary alone. The 'fact-find' also said they had a capacity to reduce their outgoings if needed. It seems to me that Mr H's aspirational spending might have been possible with a small loan, even if this was predominantly based on his civil partner's income rather than his. At the time we were in a sustained period of very low interest rates which would have meant borrowing was affordable for them but I don't think this was ever realistically considered.

- *Death benefits*

In this case, it's difficult to assess to what extent the death benefits in Mr H's DB scheme were discussed. As I've pointed out, the main rationale for the transfer advice was for access to discretionary spending by accessing his DB tax-free lump-sum once transferred. But 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. I think the evidence suggests that the issue of Mr H being in a civil partnership, as opposed to being married, was discussed. And I think the death benefits available to a spouse in his DB pension scheme may not have been available to Mr H's partner in the same way. So, I think the lump sum death benefits on offer through a personal pension were likely made to look like an attractive feature to Mr H. I think he was told that if he died, the transferred pension 'pot' would be available to Mr H's civil partner potentially tax-free. I do accept the point being made.

However, the main purpose of a pension is to fund a retirement and it could be reasonably said that Mr H's pension provision was already modest. As I've said, I do accept he'd faced a shock of having a heart attack a few months previously, but there was no indication at all that Mr H couldn't recover. There may even have been an opportunity to continue working, if only on reduced hours. But by taking this relatively small pension, withdrawing 25% of it straight away and taking annual income of £6,000 as PSA recommended, clearly there may not have been anything left for Mr H's civil partner to inherit in a personal plan at all, if he had transferred out of his DB scheme. He wasn't yet quite 55 years old and given the small extent of this CETV I think this whole pension was likely to have been run down completely within five years if Mr H followed PSA's advice. Basing the transfer on the death benefits therefore lacked credibility as they weren't really relevant.

Mr H's civil partner was also quite a bit younger than Mr H. He had his own DB pension and there was no real indication he'd be giving up working for many years. In this context, Mr H's pension wasn't quite so relevant. His civil partner enjoyed a salary and his own pension, so there was no indication that if Mr H were to die soon, his partner would necessarily suffer financial hardship.

- *Other issues*

I've seen that Mr H wanted to improve the performance of his pension. But whilst I understand most people would want to see their pension grow, this wasn't really defined or explained and it wasn't a reason to transfer. As I've shown when discussing the critical yield rates, the evidence is much more persuasive that Mr H would likely be *worse* off financially in the longer-term by transferring away.

I've also seen no evidence that Mr H had either the capacity or desire to exercise control over his funds. With his DB scheme, Mr H had a guaranteed income for life and the scheme was run for him by trustees. The evidence I've seen shows Mr H himself had no experience of these types of other DC 'money market' investments and I think he would have found the complexity of managing the transferred funds to be onerous in the years ahead. What I've seen tends to show Mr H would have required ongoing financial advice and support, all of which would cost him money which his DB scheme didn't require from him.

Suitability of investments

PSA recommended that Mr H invest his funds in a personal pension. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Mr H and I don't think he would've insisted on transferring out of the scheme if clear advice had been given to him, it follows that I don't need to consider the suitability of the investment recommendation. This is because he should have been advised not to transfer and so the investment in the new funds wouldn't have arisen if suitable advice had been given.

Summary

I don't think the advice PSA gave Mr H to transfer away from his DB scheme was suitable.

Even though Mr H had two DB pensions, he had what could be reasonably described as only modest pension provisions overall. With this smaller scheme, he was giving up a risk-free, known and guaranteed pension for life. PSA failed to explain to Mr H the relevance of the critical yield rates which showed he was likely to receive lower pension benefits as a result of transferring away.

There were also no other credible reasons to transfer the pension. PSA hung its recommendation on a desire for flexibility which was both poorly defined and simply not required. In fact, the evidence is persuasive that Mr H's needs in retirement were for the opposite – a pension that was known to him and one which would largely keep up with the cost of living and last until he died. Whilst Mr H's partner would likely not benefit from the DB scheme's 50% 'spouse' pension, this was a relatively minor consideration particularly as the transferred funds would be quickly and entirely exhausted if following PSA's advice.

What PSA advised Mr H to do was to irreversibly transfer away from his DB scheme to fund discretionary spending which seemed somewhat vague and non-essential. Given his overall resources, the opportunity existed for the adviser to point out that either early retirement was financially unviable or that his aspirations for the apparent level of discretionary spending were unrealistic. Nevertheless, other funding methods through Mr H's civil partner's financial resources appeared more achievable and less damaging to Mr H's retirement needs.

PSA has stated at several points that Mr H was satisfied with the advice at the time and he was provided with a good amount of information. However, this is to substantially miss the point. PSA was being paid to provide this advice to Mr H, a relative amateur seeking help in this field. The adviser's job was therefore to really understand his circumstances and to provide advice that was in his best interests. The adviser made a clear recommendation for Mr H to transfer away, so not surprisingly he followed that advice.

I have considered whether Mr H would have disregarded the advice if it had been different and gone ahead with the transfer in any event. But I don't think this would have happened. The reasons given for the transfer and the release of cash were neither urgent nor essential. And I think if an adviser, which Mr H was paying for, had carefully advised him that transferring wasn't right for him I think he would have followed that advice.

In light of the above, I think PSA should compensate Mr H for the unsuitable advice. It should use the regulator's defined benefits pension transfer redress methodology.

Putting things right

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

PSA 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.

If he hadn't transferred, I accept the more plausible outcome would have been for Mr H to still access his DB pension early and in the circumstances this would have been aged 55. Compensation should be based on that retirement age. The usual assumptions in the FCA's guidance should then be used.

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 H'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, PSA should:

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

Redress paid to Mr H as a cash lump sum will be treated as income for tax purposes. So, in line with DISP App 4, PSA 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 H'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. However, this upper limit is highly unlikely to be relevant in this case.

My final decision

Determination and money award: I uphold this complaint and I direct PSA Financial Services Limited to pay Mr H the compensation amount as set out in the steps above, up to a maximum of £190,000.

If Mr H accepts this decision, the money award becomes binding on PSA Financial Services Limited.

My recommendation would not be binding. Further, it's unlikely that Mr H can accept my decision and go to court to ask for the balance. Mr H 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 Mr H to accept or reject my decision before 4 January 2024.

Michael Campbell
Ombudsman