DRN-3253672

Financial Ombudsman Service

The complaint

Mr M complained about the advice he was given by Portafina Investment Management Limited to transfer his defined benefit occupational pension to a flexi-access income drawdown pension.

What happened

In 2018 Mr M approached Portafina to get some financial advice. On 24 September 2018 Portafina issued a suitability report which outlined Mr M's current position and objectives, and Portafina's advice/recommendation and reasons for it. In summary, the report said:

Mr M's present financial position

- he was 54 and he wanted to take benefits from his pension when he turned 55
- he was married and owned his home – worth around £85,000 with an outstanding mortgage of £47,000 (with monthly repayments of £364)
- he earned approximately £26,000 a year, and was a member of his employer's pension scheme
- he had outstanding loans totalling £27,720 (with monthly repayments of £796) and an outstanding credit card balance of £500 (with monthly repayments of £50)
- he had disposable income of £508 per month.

Mr M's objectives

- to tackle his debt and to have an opportunity to be debt free
- to create an emergency fund
- to have greater flexibility about how he can access his pension in the future
- to maximise tax free cash versus the current scheme
- to have a greater choice and flexibility when it comes to death benefit• to have ownership and control of his pension fund

Alternative ways to raise funds

- a loan, re-mortgage, disposable income, assets
- the conclusion was that none of these options was viable

Required growth

- the critical yield (which is essentially the amount the new pension needed to grow by in order to match the benefits Mr M was giving up, assuming he bought an annuity) based on Mr M retiring at 65 was
    - 7.8% based on a tax free lump sum cash payment and a reduced pension being paid by the existing scheme or
    - 9.3% based on a full pension being paid
- the growth rate/hurdle rate (which Portafina describes as the amount the new pension would need to grow by for the duration of Mr M's life expectancy in order for it to

matchthe existing benefits he was giving up, assuming he remained invested in a personal pension and made withdrawals via income drawdown) was 3.1%

- Portafina said its recommendation was based on the growth rate figure, as it understood that Mr M didn't want to buy an annuity.

Underlying investments

- Mr M's attitude to risk was assessed as moderately cautious
- the recommended investment split was 40.3% fixed interest, 54.7% equities and 5% cash

Risks – various risks [of transferring] were outlined, including:

- there being a death benefit of 50% and death in service benefit of 4 x salary• the existing scheme providing guaranteed pension benefits
- the growth needed in the new pension wasn't guaranteed, and if didn't grow sufficiently Mr M's pension benefits would be lower than his existing pension.

Ultimately, Portafina recommended that Mr M transfer his pension to a flexi-access income drawdown pension so that he could access the tax-free cash available once he turned 55. His funds would be held as cash until then, at which point it would arrange for them to be invested. Portafina felt the recommendation was most suitable for Mr M given his circumstances and would provide greater benefits than his existing pension.

After receiving the advice Mr M opted out of his occupational pension, with the intention of transferring it to the pension Portafina had recommended. However, after he'd opted out he received some money through an inheritance – so he no longer needed the tax-free cash from his pension. The intended transfer didn't therefore go through. However, Mr M wasn't able to opt back into the occupational pension.

Mr M complained to Portafina as he felt the advice he'd been given was unsuitable. Portafina didn't think it had done anything wrong as the advice was based on Mr M's circumstances at the time. In any event, it said Mr M hadn't lost the benefits he'd accrued in his occupational pension as it didn't get transferred.

Our investigator concluded that the complaint should be upheld. In summary, he felt the advice was unsuitable and not in Mr M's best interests. He felt that because of the advice Mr M (by opting out of his occupational pension) lost to the ability to further contribute to the pension. Portafina disagreed with our investigator. It felt it acted fairly and reasonably, and in Mr M's best interests.

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.

Portafina has argued, in part, that Mr M didn't suffer a loss because he didn't end up transferring his pension. I think this is true to a certain extent. I say this because although Mr M opted out of his defined benefit pension he hasn't lost the benefits he accrued up to that point because he didn't end up transferring. But whether or not a loss was suffered doesn't affect whether or not the advice was suitable. In any event, Mr M might have suffered a loss because he lost the ability to remain/opt back into the defined benefit, which meant he was unable to accrue further benefits under the scheme.

My interpretation of much of what Portafina is saying overall is that its recommendation was suitable and in Mr M’s best interests because it met his objectives. I don’t think that sort of argument is persuasive. That’s because what Mr M wanted might not have been what was suitable or in his best interests (equally, what he didn’t want might have been what was suitable/in his best interests). Portafina’s advice should only have been in line with Mr M’s objectives if that was suitable and in his best interests in the short and long term – not simply because it’s what he wanted.

There were various rules and standards in place at the time that Portafina had to abide by. Two in particular that I think underpin this issue are:

- Presumption of unsuitability – Portafina was required when advising Mr M to transfer his pension to start by assuming the transfer won’t be suitable; and to then only consider it suitable if it can clearly show that it was in Mr M's best interests, and
- Fairness – Portafina was required to generally treat Mr M fairly and to act in his best interests.

While there are other factors, in most cases a key issue in me deciding whether or not advice to transfer was suitable is the critical yield, the consumer’s attitude to risk and their capacity for loss.

The suitability report gave three figures in respect of the growth needed in order to match the benefits of Mr M’s existing scheme – critical yields of 7.8% and 9.3%, and a growth rate of 3.1%. Portafina had a responsibility under the Conduct of Business Rules to consider Mr M’s attitude to risk in relation to the rate of investment growth that would have to be achieved to replicate the benefits being given up. With that in mind, I think the critical yield figures were the important ones in determining whether his pension might be worth more or less by transferring.

Portafina nevertheless chose to focus on the growth rate rather than the critical yield. Mr M’s existing scheme guaranteed him an income for life and provided a spouse’s benefit in the event of his death. I don’t think the growth rate figure provided Mr M a direct comparison with the benefits he was giving up, that Portafina needed to provide him with.

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. Businesses weren't required to refer to these rates when giving advice on pension transfers, but 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.

The closest discount rate to the time of the advice that I'm able to refer to was published by the Financial Ombudsman Service for the period before 1 October 2017 – and is 2.3% per year for one year to retirement and 3.8% for ten years to retirement. I appreciate these discount rates were from a time almost a year before the advice was given. However, industry standard projected growth rates at the time of the advice were 2% (low growth), 5% (medium growth) and 8% (high growth). It can therefore be seen that the discount rates and the low and medium growth rate figures are below the critical yields. Even the high growth rate is only just above the lowest critical yield.

Portafina said in its suitability report and in its response to our investigator that the recommended portfolio had an average return rate of 7.98% over the previous 10 years, so it expected sufficient growth on Mr M’s investments in the new pension. However, the portfolio of investments included nearly 55% in equities. Equities are risky – Portafina said itself that

they're volatile, and that the fund was category 5 (out of 7 – with 7 being the riskiest). I'm not persuaded that having such a high proportion of funds in equities matched Mr M's moderately cautious risk attitude. So while the suggested portfolio might well have achieved the growth Portafina predicted, I'm not persuaded the advice to invest in such a portfolio was suitable.

I also think Mr M's capacity for the loss of his pension was very low. The suitability report doesn't make mention of any other pensions Mr M had; and it said that after assessing his current situation it ascertained that he had no assets other than the ones outlined. I therefore think it's reasonable to conclude that, apart from the State pension, Mr M's existing pension scheme was his only source of retirement income. So any loss in the value of this pension would have a significant impact his retirement income. I don't therefore think he was in a position to take the investment risk needed in order to achieve the required growth. And I don't think he had sufficient capacity to absorb any loss of his pension provisions.

Given the above, I think it was unlikely the new pension would grow sufficiently in order to match the benefits Mr M was giving up. I say this because Mr M had been assessed as having a moderately cautious attitude to risk; and I'm not persuaded given the discount rates and industry standard projected growth rates that any investment that suitably matched this profile would grow sufficiently.

I'm also concerned with some of the reasons Portafina gave for concluding that the advice was suitable. In my view, the overriding reason for the recommendation was that it would enable Mr M to access a tax-free lump sum cash payment, which he could then use to pay off some debts. However, Mr M couldn't access that cash until he turned 55. So I think any advice ought to have been delayed until Mr M could actually access the cash. Also, although the suitability report said there weren't any other viable options to raise the cash, and that the only viable way for Mr M to raise funds was to re-mortgage (which would have defeated the object of reducing his debts), I haven't seen anything showing that any analysis was done in this respect. For example, I appreciate the amount of debt might have been the same, but consolidating the debt by re-mortgaging might have reduced the overall outgoings (especially considering low interest rates at the time).

Other reasons included that Mr M could vary his income and take ownership and control of his pension. But I haven't seen any analysis of how likely it was that Mr M would actually do this and, more importantly, how this would be in his best interests and make the advice suitable.

Portafina made various comments in response to our investigator's opinion. I believe I've covered most of them with my comments above. There are nevertheless some points that I will specifically address:

- Mr M's debt repayments were more than half of his monthly wage and by clearing them he would increase his disposable income and improve his financial situation ready for retirement – I think this is a short-sighted approach; it may be that Mr M's immediate financial position would be improved by reducing his debts, but that loses sight of what his financial situation would be at/after retirement (which, after all, is what a pension is for); and, as I've said above, Mr M was only 54 at the time so he couldn't have taken the tax-free cash at that point anyway
- although Mr M was able to meet the monthly debt repayments there was a risk that his income may reduce eg due to his overtime being reduced or his wife losing her temporary work – I accept this was the case; however, if it happened Mr M could have got further advice at that point
- reference was made to Mr M feeling that the only way he could clear his debt was by taking money from his pension – Portafina's role was to provide suitable advice, not to

provide advice based on what Mr M's feels; what Mr M feels and what was actually suitable might well be two different things
- based on past performance of the recommended portfolio the average annual rate of return over the previous 10 years was 7.98%, which was higher than the hurdle rate and critical yield, so Portafina felt it could be matched – I have no reason to disbelieve what Portafina says about the past performance, but that argument does somewhat go against warnings in the suitability report that past performance is no guarantee of future performance
- the trustees of Mr M's existing scheme could have used their discretionary power and allow him to opt back into the scheme, so the trustees could have done more to resolve this issue and any complaint regarding Mr M re-joining should be directed to the trustees – whether Mr M wishes to complain to/about the trustees is his prerogative; the complaint I'm considering isn't about that though, it's about the advice Portafina gave Mr M to transfer.

With all the above in mind, I conclude that Portafina's advice to Mr M in September 2018 was unsuitable.

I haven't seen anything which suggests to me that Mr M was an experienced or sophisticated investor. So I think it's reasonable to conclude that he was reliant on the advice he received, and that he would most likely have heeded it. On that basis, I think it's most likely that if Portafina had provided suitable advice Mr M wouldn't have opted out of his existing pension. He wouldn't therefore have found himself in the position he now found himself in when he received his inheritance.

Putting things right

A fair and reasonable outcome is for Portafina to put Mr M, as far as possible, into the position he would now be in but for the unsuitable advice. I consider he would have remained in the occupational scheme. Portafina must therefore undertake a redress calculation in line with the regulator's pension review guidance as updated by the Financial Conduct Authority in its "Finalised Guidance 17/9: Guidance for firms on how to calculate redress for unsuitable DB pension transfers".

This calculation should be carried out as at the date of my final decision, and using the most recent financial assumptions at the date of that decision. In accordance with the regulator's expectations, this should be undertaken or submitted to an appropriate provider promptly following receipt of notification of Mr M's acceptance of the decision.

Portafina may wish to contact the Department for Work and Pensions ("DWP") to obtain Mr M's contribution history to the State Earnings Related Pension Scheme (SERPS or S2P). These details should then be used to include a 'SERPS adjustment' in the calculation, which will take into account the impact of leaving the occupational scheme on Mr M's SERPS/S2P entitlement.

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Mr M's current pension plan. The payment should allow for the effect of charges and any available tax relief. The compensation shouldn't be paid into the pension plan if it would conflict with any existing protection or allowance.

If a payment into the pension isn't possible or has protection or allowance implications, it should be paid directly to Mr M as a lump sum after making a notional deduction to allow for income tax that would otherwise have been paid. Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to Mr M'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.

The compensation amount must where possible be paid to Mr M within 90 days of the date Portafina receives notification of his acceptance of my final decision. Further interest must be added to the compensation amount at the rate of 8% per year simple from the date of my final decision to the date of settlement for any time, in excess of 90 days, that it takes Portafina to pay Mr M.

It's possible that data gathering for a SERPS adjustment may mean that the actual time taken to settle goes beyond the 90 day period allowed for settlement above – and so any period of time where the only outstanding item required to undertake the calculation is data from DWP may be added to the 90 day period in which interest won't apply.

My final decision

I uphold this complaint. I require Portafina Investment Management Limited to settle this matter as outlined under the "Putting things right" heading above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 14 February 2022.

Paul Daniel
Ombudsman