DRN-4182077

Financial Ombudsman Service

The complaint

Mr R complains about the advice given by Portafina Investment Management Limited to transfer the benefits from his defined-benefit ('DB') occupational pension scheme to a self-invested personal pension ('SIPP'). He says the advice was unsuitable for him and believes this has caused a financial loss.

What happened

Mr R contacted Portafina in 2018 to discuss his pension and retirement needs. I understand that Mr R saw an online advertisement for Portafina about pension transfers, and registered his interest about a transfer. Portafina then contacted him following this.

Portafina completed a telephone fact-find to gather information about Mr R's circumstances and objectives. This showed, and Mr R has also explained as part of the complaint, that he:

- Was aged 54 and employed, he'd been in the same employment for 21 years and he was earning £25,000.
- Was a member of his employers DB scheme.
- Was living with his partner but had no dependents.
- Had no financial assets.
- Was renting a council property which was costing him £400 a month.
- Had an unsecured loan to which he was paying £170 a month.
- Had disposable income of £230 a month

Mr R received a Cash Equivalent Transfer Value ('CETV') for the benefits he held in the DB scheme. The amount shown on the suitability report was £110,769. Mr R also had some additional voluntary contributions ('AVC'). The AVC had a CETV of £5,606.08.

It's worth noting here that when the DB transfer went ahead the CETV had increased to £122,266.83.

Portafina also carried out an assessment of Mr R's attitude to risk, which it said was 'cautious' and that he had a low capacity for loss. The DB scheme was his main pension provision.

On 4 February 2019, Portafina advised Mr R to transfer his pension benefits into a SIPP and invest the proceeds. The SIPP invested in the providers global short dated bond fund and it's world equity funds. The suitability report said the reasons for this recommendation were that Mr R:

- Wanted to purchase his property from the council. He had the opportunity to do this at a heavily discounted price.
- Was able to opt back into his DB scheme following the transfer to enable him to continue to benefit from his employers contributions.
- Didn't want to borrow to fund the house purchase, and he couldn't buy the house using his disposable income

Mr R complained in 2022 to Portafina about the suitability of the transfer advice. He said that:

- He wasn't made aware of the benefits he would be losing by transferring out of the DB scheme and the advice wasn't properly explained
- He used the tax-free cash to put a deposit down on his home. However, he says no alternatives, such as loans, were offered to this by Portafina.
- He didn't think he was able to make an informed decision about what options he had.
- The DB scheme was Mr R's main source of retirement income so he could not afford to lose it and wasn't looking to take any risk with his pension.
- Mr R thinks the transfer exposed him to unnecessary risk.

Portafina didn't uphold Mr R's complaint. It said that the council had offered Mr R a greatly discounted price to purchase the council property that he was renting. He could purchase the house for £50,000 and the market value of it was £110,000. So, Mr R would achieve an immediate gain on the transfer and he would free up a significant amount of disposable income. He was also able to opt back into the DB scheme following the transfer so would be able to accrue further DB scheme benefits. Portafina thinks the transfer was in Mr R's best interests.

Mr R referred his complaint to our service. An Investigator upheld the complaint and recommended that Portafina pay compensation. Our Investigator said that Mr R was very likely to receive much lower benefits at retirement than he would have done from the DB scheme. And it's likely that he would have been able to purchase his council properly using other means rather than use his pension. The other advantages of the DB Transfer, such as better death benefits, weren't enough to outweigh the reduction in retirement benefits.

Portafina disagreed, saying:

- It wasn't aware that Mr R part financed his property purchase with a loan. The fact find showed that he had no savings or spare income, and was bankrupt some time ago, so he may have found this difficult to do.
- In a fact find call Mr R had said that he did not want to finance his house purchase by taking a loan.
- As he used the pension to purchase the house he saved on rental payments. It would not make financial sense to have used a mortgage to do this.
- Mr R said that as he could purchase the property at a 62% discount it was a 'no brainer'.
- He was happy to take the risk of the pension and he wanted to buy his council property.
- The death benefits were an ancillary need and not as important as the house purchase.
- Mr R opted back into his employer's scheme.

The Investigator wasn't persuaded to change their opinion, so the complaint was referred to me to make 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 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 Portafina'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, Portafina should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr R’s best interests. And having looked at all the evidence available, I’m not satisfied it was in his best interests.

Financial viability

Portafina calculated a transfer value comparator (TVC). This was required by the regulator on transfers after 1 October 2018 - and is a calculation of the funds that would need to be invested at the time of transfer on a so-called 'risk-free' basis, to provide the same income as the DB scheme at normal retirement age. It said this was £263,970 which was £158,919 more than the transfer value.

Petrofina also calculated how much Mr R’s pension fund would need to grow by each year in order to provide the same benefits as his DB scheme (the critical yield).

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.

Mr R was 54 at the time of the advice and wanted to retire at 67. The critical yield required to match Mr R's benefits at his retirement age was 10%. It's not clear if this was on the basis that Mr R was taking tax-free cash or not. The critical yield fell to 8.3% when the transfer value was increased to £122,266.89.

The relevant discount rate closest to when the advice was given which I can refer to was published by the Financial Ombudsman Service for the period before 1 October 2017, and was 3.9% per year for 11 years to retirement. I've kept in mind that the regulator's projection rates had also remained unchanged since 2014: the regulator's upper projection rate at the time was 8%, the middle projection rate 5%, and the lower projection rate 2%.

I've taken this into account, along with the composition of assets in the discount rate, Mr R's 'low' attitude to risk and also the term to retirement. There would be little point in Mr R giving up the guarantees available to him through his DB scheme only to achieve, at best, the same level of benefits outside the scheme. But here, given the lowest critical yield was 8.3%, I think Mr R was likely to receive benefits of a substantially lower overall value than the DB scheme at retirement, as a result of investing in line with that attitude to risk.

Portafina has provided cashflow models which it says show Mr R would've been able to meet his needs despite the high critical yields. I've considered these, but Portafina's models show that if Mr R lived to 95, and the fund grew at 5.8%, then it would run out at this age. So Mr R could run into problems if he lived a long time or investment returns were much lower than this. And bearing in mind Mr R's lower attitude to risk he would probably expect returns below 5.8%, and so the funds lasting to his age of 95 seems optimistic.

Also, as Portafina will know, past performance is no guarantee for future performance and so I consider the discount rates and the regulator's standard projections to be more realistic in this regard in the long term rather than projecting historic returns forward, particularly over such a long period of time.

So, as a starting point here, a transfer out of the DB scheme wasn't in Mr R's best interests. Of course, financial viability isn't the only consideration when giving transfer advice, as Portafina has said in this case. Portafina thinks there are other considerations which mean the transfer was suitable, despite providing overall lower benefits. It has said that the benefit to Mr R of purchasing his council house outweighed the pension income he was giving up. I've considered this below.

Flexibility and income needs

Mr R wanted to take his pension flexibly in order to purchase his property and the decision was closely linked to the financial viability of the transfer. Portafina essentially thinks that Mr R's ability to purchase his property at a discount made the transfer viable.

Portafina does not seem to have established what Mr R's needs in retirement were. I don't think it properly looked at what Mr R wanted as income, or what he thought his expenditure would be, in his retirement. It did ask some very brief questions about what expenditure he

had that may continue into his retirement, but no more than this. It didn't compare this with his expected retirement income at all. I can't see how it could effectively have advised Mr R on his retirement when this was the case. And this is what it really should have been concentrating on when giving DB transfer advice. One of the main considerations should have been how the transfer would affect Mr R's retirement planning. And it was a serios failing of Portafina's that it didn't do this.

Portatafina advised Mr R on the basis that he wanted to purchase his house and he should use his DB scheme funds to do this. Clearly Mr R did want to do this, and it's also clear why. But his pension was there to fund his retirement and shouldn't have been the default choice for funding, as it seems to have been here.

I've looked at the financial viability of this above, but Portafina has said that the transfer was in his best interests due to the discounted price which he could purchase his house. Essentially this was because the house was valued at £110,000 and Mr R could purchase it for £50,000. And he would also not have to pay rent, which was £400 a month, going forward.

But this doesn't tell the whole story. On the one hand Mr R would gain the estimated £60,000 increase in the house value and Portafina said he would save rental income of £57,000 (to his retirement). So there are gains here. But Portafina also estimated that Mr R would need a fund of £263,970, which was £158,919 more than the transfer value, to replicate the benefits he was giving up. And so the cost to him, even with house price valuations and the rent estimates was still greater than the benefits he was giving up. Of course, these are all estimates but I think it's reasonable to say that they demonstrate that using the DB transfer in this way didn't make financial sense.

The usual way to purchase a house is to borrow. I can see this was discussed with Mr R and he didn't want to do this. Of course, the DB transfer would have seemed like a far easier way to get what he wanted. And he would no longer have to pay rent or take out a mortgage. So, this isn't surprising.

But I think Portafina should have fully considered, and looked into how, Mr R could fund the house purchase another way because of the overall cost to him. It doesn't seem to have investigated this in any detail at all. This is dealt with very briefly in the calls I've listened to and the representative simply accepts when Mr R says he 'doesn't want to go down this route', rather than explaining that this may be a good way to fund the house purchase.

On the face of it, Mr R did have some time until retirement, the house price was modest and he did already have some credit. So, it looks likely it would have been possible for him to borrow. And it could have been considered, for example, whether Mr R could have borrowed in an interest only basis and used the tax-free cash to repay this at the schemes normal retirement date. Portafina should have fully explored this, or referred him to an adviser that could. I think if Portafina had done this it's likely that Mr R would have been able to fund the house purchase another way.

I've listened to the calls that Portafina has provided. Mr R and Portafina spoke about his circumstances, and the house purchase, and the guaranteed pension he was giving up. But it seems unclear to me that Mr R fully understood what he was entering into. He was aware that he was giving up a guaranteed pension, but he seems to be under the impression that he would replace this by re-joining the scheme, which isn't the case.

And I think that he didn't understand the value of what he was giving up. The advantages are clear to him, but the discussion concentrated on the gains from the house purchase, I can't see the amounts calculated as part of the TVC were ever discussed. Portafina made no

attempt to inform him about this in the calls. I don't think it acted fairly here, and I'm not persuaded that Mr R would have proceeded if it had done this.

Overall, I don't think Mr R required flexibility in retirement. This is because based on the evidence I've seen, I don't think he had a genuine need to access his tax-free cash earlier than the normal scheme retirement age and leave his funds invested until a later date. I also can't see that Mr R had a strong need for variable income throughout his retirement. This doesn't seem to have been discussed.

Mr R's DB scheme was projected to provide an annual pension of £9,242 from the age of 67, or a reduced pension of £6,041 if he took tax-free cash of £40,274. He would also have his state pension on top of this.

I don't know exactly what Mr R's needs would be in retirement. But I still think he could have best met his retirement income needs by remaining in the DB scheme until the state pension became payable. I don't think the transfer was suitable due to Mr R's want for flexibility and the associated house purchase.

Death benefits

It was recorded that Mr R wanted to improve on the death benefits he could provide to his partner.

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 R. But whilst I appreciate death benefits are important to consumers, and Mr R might have thought it was a good idea to transfer his DB scheme to a personal pension because of this, the priority here was to advise Mr R about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think Portafina explored to what extent Mr R was prepared to accept a lower retirement income in exchange for higher death benefits.

It's not clear if the DB scheme would have provided any death benefits, given that he wasn't married to his current partner. But in any event, Portafina should not have encouraged Mr R to prioritise the potential for higher death benefits through a personal pension over his security in retirement.

Furthermore, if Mr R genuinely wanted to leave a legacy for his spouse, which didn't depend on investment returns or how much of his pension fund remained on his death, I think Portafina should've instead explored life insurance.

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

Control or concerns over financial stability of the DB scheme

I think Mr R's need for control over his pension benefits was overstated. Mr R 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 his own. So, I don't think that this was a genuine objective for Mr R – it was simply a consequence of transferring away from his DB scheme.

The funding of his employer's DB scheme was not in a position such that Mr R should have genuinely been concerned about the security of his pension. I note that Mr R was encouraged to re-join this going forward and I understand that he did.

Suitability of investments

Portafina recommended that Mr R invest in two risk bearing funds. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Mr R, it follows that I don't need to consider the suitability of the investment recommendation. This is because Mr R should have been advised to remain in the DB scheme and so the investments in the funds wouldn't have arisen if suitable advice had been given.

Summary

I don't doubt that the flexibility, control and potential to easily purchase his property at a discount would have sounded like attractive features to Mr R. But Portafina wasn't there to just transact what Mr R might have thought he wanted. The adviser's role was to really understand what Mr R needed and recommend what was in his best interests.

Ultimately, I don't think the advice given to Mr R was suitable. He was giving up a guaranteed, risk-free and increasing income. By transferring, Mr R 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 R shouldn't have been advised to transfer out of the scheme just to purchase his property, and the potential for higher death benefits wasn't worth giving up the guarantees associated with his DB scheme.

So, I think Portafina should've advised Mr R to remain in his DB scheme.

Of course, I have to consider whether Mr R would've gone ahead anyway, against Portafina's advice.

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

I'm not persuaded that Mr R's want to purchase his property was so great that he would've insisted on the transfer knowing that a professional adviser, whose expertise he had sought out and was paying for, didn't think it was suitable for him or in his best interests. If Portafina had looked into how Mr R could meet all of his objectives without risking his guaranteed pension, I think that would've carried significant weight. So, I don't think Mr R would have insisted on transferring out of the DB scheme.

In light of the above, I think Portafina should compensate Mr R 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 the business to put Mr R, as far as possible, into the position he would now be in but for the unsuitable advice to transfer the DB scheme and the AVC. I consider Mr R would have most likely remained in the occupational pension scheme if suitable advice had been given.

Portafina 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 R 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, 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 R'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, Portafina should:

- calculate and offer Mr R redress as a cash lump sum payment,
- explain to Mr R before starting the redress calculation that:
    - his 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 his redress prudently is to use it to augment his DC pension
- offer to calculate how much of any redress Mr R receives could be augmented rather than receiving it all as a cash lump sum,
- if Mr R accepts Portafina's offer to calculate how much of his redress could be augmented, request the necessary information and not charge Mr R 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 R's end of year tax position.

Redress paid to Mr R 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, Portafina 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 R'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.

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My final decision

Determination and money award: I uphold this complaint and require Portafina Investment Management Limited to pay Mr R 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 Portafina Investment Management Limited pays Mr R the balance.

If Mr R accepts this decision, the money award becomes binding on Portafina Investment Management Limited.

My recommendation would not be binding. Further, it's unlikely that Mr R can accept my decision and go to court to ask for the balance. Mr R 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 R to accept or reject my decision before 4 August 2023.

Andy Burlinson
Ombudsman