DRN-4378320

Financial Ombudsman Service

The complaint

Mr W has complained that Lighthouse Advisory Services Limited (Lighthouse) gave him unsuitable advice to transfer his defined benefits from his occupational pension scheme (OPS) to an income withdrawal plan.

What happened

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

In November 2007 Mr W contacted his scheme provider for details of the benefits associated with his defined benefit OPS. The trustees offered him a financial incentive to transfer his pension benefits to a personal pension. Mr W was referred to Lighthouse to consider his options further.

Lighthouse completed a fact find analysis on 12 December 2007 to establish Mr W's circumstances and financial objectives. It recorded that:

- Mr W was 50 years old, married and had no financial dependants. He was employed full time and didn't plan to retire until age 70.
- Mr W owned his own home which had an outstanding mortgage of £90,000 and was due to be repaid in 20 years.
- He had £20,000 in savings. The fact find also referred to credit card liabilities costing £300 per month.
- Mr W was a deferred member of the defined benefit scheme with 19 years of service. His pension had a transfer value of £62,940 and would pay him a guaranteed annual income of £5,771 pa once he reached age 60.
- The scheme offered him an incentive of £35,773 if he transferred out of the scheme at the time of advice, making the final transfer value £98,723.
- Lighthouse didn't note any other pensions or retirement provisions held by Mr W.
- An assessment of Mr W's attitude to risk determined that his risk appetite was balanced. His capacity for loss was low.

Lighthouse issued a suitability report dated 31 March 2008. It recommended Mr W transfer his defined benefits to a Legal and General income withdrawal plan. Lighthouse recorded that Mr W had the following key objective:

- Mr W wanted to use the tax free cash available from the transfer and his savings to reduce his mortgage burden, which had been causing him some concern.

But Mr W was also recorded as having the following priorities:

- *"You wish to break all ties with your ex employer and would prefer to move your funds to an individual plan under your control.*
- *These benefits are a major proportion of your pension funding which should be protected as far as possible.*

- *You have very little life insurance, and your dependants could do with extra sums if they were available.*
- *You would like the flexibility at retirement to control the way benefits are paid.*
- *You require the maximum possible lump sum at the earliest opportunity.*
- *You plan to retire at age 70.*
- *You do not mind a reasonable degree of risk in the hope for higher benefits in retirement."*

Lighthouse recommended that Mr W use £24,678 in tax free cash and his £20,000 savings to reduce his mortgage. It also recommended that Mr W withdraw a monthly amount of £300 and reinvest this into a personal pension policy (PPP).

Mr W accepted Lighthouse's recommendation and the transfer proceeded in May 2008.

In February 2023 Mr W made a formal complaint to Lighthouse. Mr W explained that he had unfortunately had to retire due to ill health and he now found himself reliant on his wife as his pension didn't provide a useful benefit. He said that he now realised that if he'd stayed in the defined benefit pension scheme, he would be much better off financially.

Lighthouse declined to uphold Mr W's complaint, however. It said that its recommendation was clear and Mr W was financially better off as he'd offset his mortgage debt which would have cost him a lot more over the years.

Unhappy with this response, Mr W referred his complaint to this service.

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

- With regard firstly to the jurisdiction of this service to consider the complaint – and specifically the timeliness of Mr W raising his complaint in accordance with DISP 2.8.2R - Mr W's complaint had clearly been made more than six years after the advice had been given. But in terms of whether Mr W had complained within three years of when he became aware, or ought reasonably to have become aware, of having cause for complaint, there'd been no extreme reductions in the value of Mr W's plan over the time he'd been withdrawing from it. And the withdrawals would have meant it was difficult to compare the value of the drawdown plan with the scheme benefits had he retained them. Mr W had said that it was only when he came to retire due to ill health that he became concerned about his pension benefits. As such, and in the absence of other evidence which might suggest that Mr W ought to have been aware of having cause for complaint more than three years before he complained, the complaint was one we could consider.

- In terms of the merits, 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 given during the period when 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 discount rate was 6.4% pa for the period up to Mr W's normal retirement date. The regulator's low, mid and upper band projected annual growth rates were 5%, 7% and 9% respectively.

- This compared to a required critical yield to match the scheme benefits at 65 of 6.7% pa.

- Mr W had no other significant assets or other anticipated sources of income in retirement. He therefore had no capacity to absorb losses on the pension transfer.

- Talking this into account, in addition to the composition of assets used to determine the discount rate, Mr W's attitude to risk, and his term to retirement, it was likely that he would receive benefits of a materially lower overall value by transferring.

- The recommendation was given so that Mr W could reduce his mortgage, but although this may have been a desirable course of action, it was Lighthouse's responsibility to do more than simply transact Mr W's preferred course of action.

- Mr W was able to meet his monthly mortgage payments, there were no arears, and he was in fact able to save on a monthly basis from his income. There was therefore no immediate need to reduce the mortgage.

- Alternatives such as using the surplus income to make overpayments weren't explored, and it was likely that Mr W was charged a significant fee for reducing his mortgage by almost half.

- Mortgage repayment shouldn't therefore have been considered a greater priority than securing his guaranteed scheme benefits in retirement. Mr W had no other pension provision and so Lighthouse should have advised Mr W to protect his defined benefits.

- Lighthouse had said that the transfer provided Mr W with flexibility of income, but Mr W demonstrated no need for this at the time of the advice. He said that he didn't need an income whilst still working, and so it was to his detriment that he transferred to an arrangement which enabled him to take frequent withdrawals. The maximum pension should have been preserved for retirement.

- The enhancement – and a means of reducing his mortgage - would have been appealing to Mr W, but the transfer wasn't in Mr W's best interests.

The investigator recommended that Lighthouse undertake a loss calculation in accordance with the regulator's consultation paper CP22/15.

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

Mr W accepted the investigator's assessment. Lighthouse didn't, however, asking for the matter to be referred to an ombudsman for review, but it provided no further commentary or submissions.

As agreement hasn't been reached on the matter, it's now been referred to me.

What I've decided – and why

Lighthouse hasn't commented specifically on any aspect of the investigator's findings, including our jurisdiction to consider the matter, but I'd firstly say that, having considered whether this case falls within our jurisdiction, I'm satisfied that it does.

I agree with the observations made by the investigator. Although the complaint was raised more than six years after the advice was given, I don't think that, under the second limb of DISP 2.8.2R, the available evidence supports the position that Mr W either was aware, or ought reasonable to have been aware, that he had cause for complaint, more than three years before he raised his complaint.

I think it's a credible position that it was only when Mr W came to retire through ill health that he wondered whether the benefits he would have received from the scheme might have been higher than those he would receive from the transfer.

And as this was fewer than three years before he raised his complaint, under the provisions of DISP 2.8.2R, I'm satisfied that the complaint therefore falls within our jurisdiction.

As with the investigator, I've then proceeded to consider the merits of the complaint.

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

And having done so, I've reached similar conclusions to those set out by the investigator, and for broadly the same reasons.

When considering what's fair and reasonable, and in accordance with the Financial Services and Markets Act 2000 (FSMA) and DISP, I need to take into account relevant: law and regulations; regulators' rules, guidance and standards, and codes of practice; and, where appropriate, what I consider to have been good industry practice at the time.

The applicable guidance, rules, regulations and requirements

This isn't a comprehensive list of the guidance, rules and regulations which applied in 2008, but provides useful context for my assessment of the business' actions here.

Within the FSA's handbook, COBS 2.1.1R required a regulated business *to "act honestly, fairly and professionally in accordance with the best interests of its client".*

The FSA's suitability rules and guidance that applied at the time Lighthouse advised Mr W were set out in COBS 9. The purpose of the rules and guidance is to ensure that regulated businesses, like Lighthouse, take reasonable steps to provide advice that is suitable for their clients' needs and to ensure they're not inappropriately exposed to a level of risk beyond their investment objective and risk profile.

In order to ensure this was the case, and in line with the requirements COBS 9.2.2R, Lighthouse needed to gather the necessary information for it to be confident that its advice met Mr W's objectives and that it was suitable. Broadly speaking, this section sets out the requirement for a regulated advisory business to undertake a "fact find" process.

There were also specific requirements and guidance relating to transfers from defined benefit schemes – these were contained in COBS 19.1.

COBS 19.1.2R required the following:

"A firm must:

(1) compare the benefits likely (on reasonable assumptions) to be paid under a defined benefits pension scheme with the benefits afforded by a personal pension scheme or stakeholder pension scheme, before it advises a retail client to transfer out of a defined benefits pension;
(2) ensure that that comparison includes enough information for the client to be able to make an informed decision;
(3) give the client a copy of the comparison, drawing the client's attention to the factors that do and do not support the firm's advice, no later than when the key features document is provided; and
(4) take reasonable steps to ensure that the client understands the firm's comparison and its advice."

Under the heading *"Suitability"*, COBS 19.1.6 set out the following:

"When advising a retail client who is, or is eligible to be, a member of a defined benefits occupational pension scheme whether to transfer or opt-out, a firm should start by assuming that a transfer, conversion or opt-out will not be suitable. A firm should only then consider a transfer or opt-out to be suitable if it can clearly demonstrate, on contemporary evidence, that the transfer or opt-out is in the client's best interests."

COBS 19.1.7 also said:

"When a firm advises a retail client on a pension transfer or pension opt-out, it should consider the client'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."

And COBS 19.1.8 set out that:

"When a firm prepares a suitability report it should include:

(1) a summary of the advantages and disadvantages of its personal recommendation;

(2) an analysis of the financial implications (if the recommendation is to opt-out); and

(3) a summary of any other material information."

I've therefore considered the suitability of Lighthouse's advice to Mr W in the context of the above requirements and guidance, and would comment as follows.

The transfer value analysis which Lighthouse was required to carry out by the regulator said that the critical yield - how much Mr W's pension fund would need to grow by each year in order to provide the same benefits as his defined benefit scheme – was 6.7% to age 65. This was after tax free cash was taken into account. The critical yield to match the scheme benefits at 65 with no tax free cash being taken was 7.7%.

The discount rate was 6.4% to age 65, and the regulator's middle projection rate for growth was 7% pa. On the face of it, if Mr W was intending to take the full tax fee cash entitlement at retirement, I think the matter of financial viability was quite finely balanced. But the critical yield is the growth that the transferred funds would need to achieve, year on year, to simply match the scheme benefits. For the transfer to be worthwhile from a financial perspective, there needed to be a realistic prospect that the transfer would result in greater benefits for Mr W.

I don't think this could be clearly demonstrated here. And so, as with the investigator, I think Mr W was more likely than not to receive pension benefits, from 65 (although I acknowledge that Mr W didn't plan to retire until age 70), of a lower value, or perhaps at best around the same (but without the guarantees), than those he'd have been entitled to under the scheme by transferring and investing in line with his balanced attitude to risk.

I can see from the suitability report that it was in any case envisaged that Mr W would withdraw tax free cash immediately and being taking income withdrawals. The objective of Mr W taking income withdrawals, beyond the tax free cash to repay part of his mortgage, was to recycle this into a PPP. This would be £300 pm, which would then provide for further tax free cash.

But this was a fairly complicated, circuitous process, especially for an inexperienced investor - and it required some discipline. And whilst it may have offered some tax advantages, the actual return would in any case be subject to the investment performance of the contributions made. Given the valuable guaranteed benefits which Mr W would be relinquishing by transferring and embarking upon this course of action, and his low capacity for loss, I don't think on a reasonable analysis of Mr W's situation, it could be justified.

My understanding is that this didn't in any case happen. Mr W found the concept confusing and didn't understand why he had two plans. He didn't begin withdrawals until 2018, when he first began experiencing health issues for which he was hospitalised.

As noted by the investigator, Mr W may have considered the prospect of accepting the cash enhancement and reducing his mortgage to be appealing, but he was able to service the mortgage and also able to save on a monthly basis from his surplus income. As such, there appears to have been no particular need for Mr W to transfer for this purpose and relinquish valuable guaranteed benefits.

Mr W was recorded as having a low capacity for loss, given in large part his lack of other pension provision, and was also recorded as wishing to protect his pension benefits as far as possible. This wouldn't sit at all comfortably with a transfer of the defined benefits, which were guaranteed and would have received revaluation up to retirement and would then escalate post retirement.

The investigator observed that financial advice isn't simply concerned with wish fulfilment – and I agree. As I've said above, Mr W may have found the prospect of mortgage reduction appealing, albeit with an unknown fee which might usually have been levied for this kind of overpayment, but it was the responsibility of Lighthouse to explore alternatives to this which would mean that Mr W could retain his defined benefits. And as commented by the investigator, this could have taken the form of regular overpayments from surplus income.

I also haven't seen persuasive reasons as to why Mr W would need the flexibility of income which would be provided by the transferred funds in retirement, when compared against the guaranteed escalating income which he would receive from the scheme.

In terms of the alternative lump sum benefits a transfer offered to his family, the priority here was to advise Mr W about what was best for his retirement. And the existing scheme offered death benefits, by way of a spouse's pension, which would have been valuable to his wife in the event of his death.

Whilst the CETV figure would no doubt have appeared attractive as a potential lump sum, the sum remaining on death following a transfer was always likely to be different. As well as being dependent on investment performance, it would have also been reduced by any income Mr W drew in his lifetime.

Overall, I'm not satisfied that it was clearly in Mr W's best interest to relinquish his defined benefits and transfer them. And I also haven't seen anything to persuade me that Mr W 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 W received from Lighthouse was unsuitable.

Putting things right

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

I consider that Mr W would most likely have remained in the OPS if suitable advice had been given.

Lighthouse Advisory Services Limited 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.

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 W'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, Lighthouse Advisory Services Limited should:

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

- explain to Mr W 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 his defined contribution pension

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

- if Mr W accepts Lighthouse Advisory Services Limited offer to calculate how much of its redress could be augmented, request the necessary information and not charge Mr W 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 W's end of year tax position.

Redress paid to Mr W 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 W'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 Lighthouse Advisory Services Limited to pay Mr W 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 Lighthouse Advisory Services Limited pays Mr W the balance.

If Mr W accepts this final decision, the award will be binding on Lighthouse Advisory Services Limited.

My recommendation wouldn't be binding on Lighthouse Advisory Services Limited. Further, it's unlikely that Mr W could accept my decision and go to court to ask for the balance. Mr W may want to consider getting independent legal advice before deciding whether to accept my final decision.

In Mr W's complaint to Lighthouse Advisory Services Limited in early 2023, he explained his health conditions and the impact the matter had caused him. Lighthouse Advisory Services Limited acknowledged this in its final response letter, saying that it understood the stress and concern Mr W had experienced.

I've therefore also taken into account whether a payment in respect of this would be warranted here. It's fair to say that, as Mr W has said that he only became aware of cause for complaint when he recently needed to retire through ill health, he won't have experienced a prolonged period of uncertainty as to whether the advice from 2008 has resulted in financial loss for him. And the above calculation will determine whether Mr W has in fact incurred a financial loss by transferring. But I do think that concerns over the matter will have exacerbated his already difficult circumstances.

As such, on the basis that I've concluded above that the transfer advice was unsuitable, and as Lighthouse Advisory Services Limited has itself acknowledged Mr W's stress and concern caused by the matter, I think it should pay to him £250 in respect of this.

My final decision

My final decision is that I uphold the complaint and direct Lighthouse Advisory Services Limited to undertake the above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr W to accept or reject my decision before 31 January 2024.

Philip Miller
Ombudsman