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Appendix 4 Handling pension transfer redress calculations

4.3 Steps for redress calculation

App 4.3.1 R A *firm* must take the 5 steps set out in this section to carry out a redress calculation.

App 4.3.2 G The diagram at DISP App 4 Annex 3 explains the 5 steps for the redress calculation in diagrammatic form, with reference to the relevant sections of the *rules* and *guidance*. To the extent there is any inconsistency between the diagram and the *rules*, the *rules* will prevail.

Step 1: obtain the necessary information to calculate redress

App 4.3.3 R The first step is for the *firm* to obtain the necessary information about the *consumer's*:

(1) DC pension arrangement;

(2) *defined benefit occupational pension scheme* or, if there is more than one *defined benefit occupational pension scheme*, the one which the *consumer* would most likely have had rights in if they had received compliant pension transfer advice determined in accordance with DISP App 4 Annex 1 16.1G to 16.5G;

(3) personal and financial situation; and

(4) preference for redress to be paid either as a cash lump sum, or by full or partial augmentation where it is possible to do so without the *consumer* incurring a tax charge or liability,

to enable it to complete the redress calculation and make a redress offer.

App4.3.4 R A *firm* is entitled to rely on information previously provided by the *consumer* unless it is aware or ought to be aware that the information is out of date, inaccurate or incomplete.

App4.3.5 G Information that may be relevant to calculating redress is set out at 2.

App4.3.6 R To obtain the necessary information required to calculate or offer redress, a *firm* must:

(1) identify whether there is any relevant information held on its client file or in publicly available records; and

(2) if the information in (1) is not sufficient or could have changed:

(a) request information from the *consumer*; and

(b) with the *consumer's* permission, contact the provider of the *consumer's* DC pension arrangement and *defined benefit occupational pension scheme* and, where relevant, HMRC or DWP to obtain the information.

App4.3.7 R When offering to calculate how much redress could be paid by full or partial augmentation, the *firm* must explain to the *consumer* that:

(1) the redress offer will be calculated on the basis that the redress will be invested prudently by the *consumer*; and

(2) augmenting a defined contribution pension scheme is one way in which the redress can be invested prudently.

App4.3.8 R Requests for information in DISP App 4.3.6R must be in a *durable medium*.

App4.3.9 R The *firm* must only make requests for information that are necessary for the redress calculation that the *firm* is carrying out and, in relation to requests made to the *consumer*, information which the *consumer* can reasonably be expected to provide.

App4.3.10 R

(1) A *firm* must give a *consumer* a clear description of the information needed and explain why the information is needed to calculate redress and the consequence if the *consumer* does not provide the information.

(2) A *firm* must give a *consumer* at least 14 *days* from receipt of the request to respond to any request for information.

(3) If the *consumer* does not respond to the first request for information, or responds with insufficient information, the *firm* must make a second request for information and give the *consumer* at least 14 *days* to respond.

(4) If the *consumer* does not respond to the second request for information, or responds with insufficient information, the *firm* must contact the *consumer* again, indicating that the *firm* may have to discontinue the redress calculation if no reply is received.

(5) A *firm* may make one or more subsequent requests for information if the *consumer's* personal circumstances support the making of such further requests.

(6) A *firm* may make reasonable additional requests for information if the *consumer* requests that the *firm* calculate the redress offer by augmentation.

App4.3.11 G A *firm* should take care to adapt the procedures in DISP App 4.3.6R to 4.3.10R to the individual circumstances of the *consumer* and exercise sensitivity when requesting information about a *consumer's* personal circumstances. It may be appropriate to allow the *consumer* more time to provide a response or to make more attempts to contact the *consumer*.

App4.3.12 R If, after following the procedures in DISP App 4.3.6R to 4.3.10R, a *firm* does not have the necessary information about the *consumer's* DC pension arrangement, *defined benefit occupational pension scheme* and/or personal and financial situation to enable it to properly assess whether the *consumer* has suffered loss, the *firm* must:

(1) in the first instance, attempt to calculate redress on the basis of the information it holds; and

(2) if it is not possible to calculate redress without further information, consider whether it is appropriate to discontinue the redress calculation.

App4.3.13 G Before deciding to discontinue a redress calculation (see DISP App 4.3.12R(2)), a *firm* should consider whether it can extrapolate from information on the client file or make assumptions based on public or generic sources of information (for example, on typical retirement ages for the *consumer's* occupation) to use in the redress calculation.

App4.3.14 G A *firm* is not required to repeat a redress calculation after it has communicated a redress offer if the *consumer* subsequently provides information about their *defined benefit occupational pension scheme* or personal and financial situation which was reasonably requested by the *firm* following the procedures in DISP App 4.3.6R to 4.3.10R.

Step 2: determine when the consumer would have taken retirement benefits from the defined benefit occupational pension scheme

App4.3.15 R (1) The second step is for the *firm* to determine whether the *consumer* would have already taken retirement benefits from their *defined benefit occupational pension scheme* if, at or prior to the valuation date, they had remained a member of that scheme.

(2) To determine whether the *consumer* would have taken retirement benefits from their *defined benefit occupational pension scheme* at or prior to the valuation date, *firms* must apply the rebuttable presumption at DISP App 4.3.16R.

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App4.3.16 R A *firm* must presume that a *consumer* would have taken pension benefits from their *defined benefit occupational pension scheme* at their normal retirement age in their *defined benefit occupational pension scheme* or on death if their death preceded their normal retirement age.

App4.3.17 G The presumption in DISP App 4.3.16R will be rebutted where the evidence shows that it is more likely than not that the *consumer* or a beneficiary would have taken benefits from their *defined benefit occupational pension scheme* on an alternative date. Examples of such evidence include:

(1) the *consumer* has used some or all of their transfer proceeds to purchase an annuity; or

(2) the *consumer* would have taken early or late retirement benefits from their *defined benefit occupational pension scheme*, having regard to:

(a) the *consumer's* demands, needs and intentions at the time of the *pension transfer* advice (evidence from the time of the advice is more likely to be relevant if it shows that the *consumer* had a considered plan for taking retirement benefits early from their *defined benefit occupational pension scheme*);

(b) any information gathered by the *firm* subsequently about the *consumer's* reasons or plans for accessing pension benefits from their DC pension arrangement; and

(c) any evidence that demonstrates that the *consumer* or members of their household changed or plan to change their working pattern at a similar time to the *consumer* taking regular benefits from their DC pension arrangement; or

(3) the *firm* has written confirmation that the *consumer* considers themselves to be retired from a date which is earlier than normal retirement age.

App4.3.18 G The presumption in DISP App 4.3.16R is unlikely to be rebutted where there is:

(1) evidence from the time of the *pension transfer* advice that indicates that there is a risk that the *consumer's* intentions were influenced by the *firm's* non-compliant pension transfer advice; or

(2) evidence of irregular *pension commencement lump sum* withdrawals, particularly if the *consumer* is still working; or

(3) evidence of full withdrawal of a *pension commencement lump sum* unless:

the *pension commencement lump sum* is being or has been used for regular income payments; or

the *consumer* was in financial difficulty or in ill health at the time of the non-compliant pension transfer advice.

Step 3: carry out redress calculation

App4.3.19 R The third step is for the *firm* to calculate whether (X) is greater than (Y) on the valuation date using the formula at DISP App 4.4.2R, where:

(1) (X) is the estimated value of the benefits in the *defined benefit occupational pension scheme* together with the difference in SERPS had the *consumer* remained a member; and

(2) (Y) is the value of the benefits from the *consumer's* DC pension arrangement.

App4.3.20 R Where (X) is greater than (Y), the *consumer* has suffered a loss and the amount calculated is the primary compensation sum to be used when producing a redress offer at DISP App 4.3.29R.

Dates for calculation

App4.3.21 R The valuation date must be the first day of the quarter (for calculations undertaken within that quarter).

App4.3.22 R The redress calculation date must fall within the same quarter as the valuation date but does not have to be the same date as the valuation date.

App4.3.23 R (1) Redress calculations must be based on the new assumptions available on the first day of each new quarter, using publicly available data from the final business day of the quarter immediately before.

(2) If a *firm* carries out a further redress calculation after expiration of the validity period in DISP App 4.3.24R and 4.3.25R, including following a settlement or award made by *Financial Ombudsman Service*, that calculation must be based on the new assumptions for the quarter in which it is carried out.

App4.3.24 R Redress calculations must remain valid for 3 *months* from the date the redress offer is sent to the *consumer*, irrespective of quarterly changes to the assumptions.

App4.3.25 R A *firm* must extend the validity of the redress calculation for a reasonable period of time if there are circumstances outside of the *consumer's* control which impact on the *consumer's* ability to accept or reject a redress offer.

App4.3.26 G (1) Circumstances outside of the *consumer's* control for the purposes of DISP App 4.3.25R include:

(a) errors by the *firm* in the carrying out the redress calculation which mean the redress calculation needs to be repeated or amended by the *firm*; and

(b) exceptional personal circumstances experienced by the *consumer*, including bereavement or incapacity.

(2) Firms should ensure that they treat the *consumer* fairly when determining a reasonable time for the validity of the redress calculation to be extended by.

Step 4: work out redress offer

App4.3.27 R A *firm* must offer a *consumer* redress that, as far as possible, puts the *consumer* into the position they would have been in if they had received compliant pension transfer advice.

App4.3.28 R Redress offers must be issued to the *consumer* promptly following the calculation date and within 3 *months* of the valuation date.

Redress components

App4.3.29 R The redress must consist of the sum total of:

(1) the primary compensation sum calculated in accordance with ■ DISP App 4.3.19R and 4.3.20R, adjusted to take account of the *consumer's* tax position and any entitlement to means-tested state benefits; and

(2) a secondary compensation sum comprising any consequential losses, including any initial *adviser charges* on the DC pension arrangement and the primary compensation sum at (1) in accordance with ■ DISP App 4.3.32G, calculated using the formula at ■ DISP App 4.4.19R; and

(3) an additional compensation sum to compensate the *consumer* for the lapse of time between the valuation date and the payment date calculated in accordance with ■ DISP App 4 Annex 1 14.1G to 14.3G.

App4.3.30 R A *firm* must adjust the redress offer to take account of:

(1) the *consumer's* individual tax position, including (if the *consumer* directs that all or part of the redress be paid by full or partial augmentation) allowances on pension contributions eligible for tax relief; and

(2) the *consumer's* entitlement to means-tested state benefits.

App4.3.31 G (1) *Firms* should have regard to where the redress methodology in this appendix already factors in tax, such as when taking into account of *pension commencement lump sums*.

(2) Where redress is paid (or partially paid) by augmentation, a *consumer* will usually pay income tax when accessing their funds.

(3) A *firm* may adjust cash lump sum payments to take account of a notional deduction for tax on income from the *consumer's* pension.

(4) Where a cash lump sum payment could affect a *consumer's* entitlement to means-tested state benefits, a *firm* should take reasonable steps, with the agreement of the *consumer*, to ensure that the *consumer* does not suffer a reduction in income as a result of the redress payment. Steps that may be taken by a *firm* to prevent a *consumer* suffering a reduction in income may include:

(a) paying redress by full augmentation;

(b) paying redress as a cash lump sum up to an applicable capital or savings limit for the purposes of a state benefit eligibility means test, with the balance of the redress being paid by partial augmentation; or

(c) only after informing the *consumer* that they should seek free impartial guidance from an appropriate source, such as a Citizens Advice Bureau, cooperating with the *consumer* to put in place any arrangement, including the payment of redress in instalments over one or more future tax years:

(i) which the *consumer* has been informed would not affect their eligibility or income from means-tested state benefits;

(ii) which would not breach any regulatory requirement of the *firm*; and

(iii) if the arrangement involves the deferment of any part of the redress payable to the *consumer*, the *firm* pays an additional compensation sum in accordance with ■ DISP App 4.3.29R(3), which is calculated to the payment date in respect of the deferred part.

(5) If a *firm* has clearly informed the *consumer* of reasonable steps that may be taken to avoid a reduction in their income from means-tested state benefits, the *firm* will not be acting in breach of ■ PRIN 6 by continuing to pay redress in accordance with this appendix if the *consumer* does not agree to any of those reasonable steps being taken.

App 4.3.32 **R** Consequential losses must include the cost of initial *adviser charges* using the assumptions in ■ DISP App 4 Annex 1 9.1G if the *consumer's* assumed retirement date is after the valuation date, and:

(1) the *consumer* is not in an ongoing advice arrangement with any *firm*; or

(2) the *consumer* is in an ongoing advice arrangement with the *firm* that gave the non-compliant pension transfer advice, where;

(a) the *firm* is charging the *consumer* more than the default ongoing *adviser charges* in ■ DISP App 4 Annex 1 9.1G(2); and

(b) the *firm* will not provide an undertaking to reduce its ongoing *adviser charge* to the level of the default ongoing *adviser charge* (or lower) for the period to the *consumer's* assumed retirement date.

Means of payment

App 4.3.33 **R** (1) A *firm* must always calculate and offer to pay the total amount of redress in ■ DISP App 4.3.29R (with adjustments in ■ DISP App 4.3.30R) as a cash lump sum payment.

(2) Where a *firm* has the necessary information, the *firm* may also calculate the redress offer to be paid by augmentation without receiving a request to do so from the *consumer*.

(3) If the *firm* calculates the redress that would be paid by augmentation, it must offer the *consumer* the option of the redress being paid by augmentation or by a lump sum cash payment.

(4) If, during the period in which a redress calculation remains valid in accordance with ■ DISP App 4.3.24R to 4.3.26G, a *firm* is requested to calculate the redress payable by augmentation, it must carry out that calculation promptly.

(5) A *firm* must not charge the *consumer* for calculating how much of the redress could be paid by augmentation.

App4.3.34 G When calculating the sum that would be payable by augmentation, a *firm* must act prudently, taking account of uncertainty around the *consumer's* potential tax position at the end of the tax year, and determine the amount of the redress payment which could be paid by augmentation without exceeding the *consumer's*:

(1) allowance for personal contributions in the tax year;

(2) annual allowance, including any carry forward from previous tax years; or

(3) lifetime allowance.

App4.3.35 G (1) Factors which may be relevant to whether full or partial augmentation would result in a *consumer* exceeding their annual or lifetime allowance or allowance for personal contribution include:

(a) the *consumer's* relevant earnings in the current tax year;

(b) the value of all pension contributions already made in the current tax year;

(c) if the redress payment would result in the *consumer's* unused annual allowance in the current and previous 3 tax years being exceeded;

(d) the expected value of all pensions held by the *consumer* up to the age of 75;

(e) any lifetime allowance protections secured by the *consumer*;

(f) any applicable lifetime allowance protection enhancement factors;

(g) any benefit crystallisation events; and

(h) whether the *consumer's* money purchase annual allowance has been triggered.

(2) Unless ■ DISP App 4.3.33R(2) applies, the *firm* may make reasonable requests for information from the *consumer* where it is necessary for the *firm* to calculate the amount of redress which could be paid by augmentation.

Step 5: communicate outcome of redress calculation

App4.3.36 R The fifth step is for the *firm* to communicate the outcome of the redress calculation and any redress offer to the *consumer*.

App4.3.37 R The communication in ■ DISP App 4.3.36R must be in a *durable medium*.

App4.3.38 R The communication in ■ DISP App 4.3.36R must include the following information:

(1) An explanation of the redress calculation, including:

(a) confirmation that the redress has been calculated in accordance with the *FCA's rules* and *guidance* using an approach which has been approved by an *actuary*; and

(b) an explanation that the redress calculation takes account of the market conditions at the valuation date and this could mean that the redress might be different if it was calculated on a different date; and

(c) the information and assumptions used in the redress calculation, including:

(i) the retirement date used in the calculation; and

(ii) whether the *firm* has determined that the *consumer* would have retired in their *defined benefit occupational pension scheme* at or prior to the valuation date and if so:

(A) the basis for this determination;

(B) the impact of the determination on the valuation of the *consumer's defined benefit occupational pension scheme* (including the percentage reduction applied for early retirement) and, where the actual reduction for the *consumer's defined benefit occupational pension scheme* has not been used in the calculation, an explanation of the approach used and its impact on the redress offer; and

(C) any assumptions made about the allowance for the *pension commencement lump sum* including, where the actual commutation factors for the *consumer's defined benefit occupational pension scheme* have not been used in the calculation, an explanation of the approach used and its impact on the redress offer; and

(iii) if late retirement factors for the *consumer's defined benefit occupational pension scheme* have not been used in the calculation, an explanation of the approach used in the calculation by the *firm* and its implications for the redress offer;

(iv) the value the *firm* has placed on any illiquid or unquoted assets and the reasons for that valuation;

(v) the level of future investment returns assumed by the calculation, including an invitation for the *consumer* to review their current investment strategy to ensure it is in line with this assumption; and

(vi) the level of any charges, including product, platform and *adviser charges*, that the *consumer* is currently paying compared to the level assumed in the redress calculation, including any allowance made for initial advice from a new adviser; and

(vii) any assumption made about the *consumer's* marital or civil partnership status;

(viii) if there is more than one *defined benefit occupational pension scheme* which the *consumer* could have had rights in, the information required by 1 16.1G to 16.5G;

(ix) whether the *consumer's defined benefit occupational pension scheme* has entered or is in the Pension Protection Fund assessment period and, if so, any future increases to the value of the *consumer's* benefits which are certain and quantified, and which are known, or reasonably ought to be known, by the *firm* at the calculation date; and

(x) where *RPI*, *CPI* or earnings inflation rates are used in the redress calculation, an explanation of the published rate underlying the rate used and its source (for example, the Bank of England website) where it can be checked by the *consumer*, without any adjustment for annualisation.

(2) An explanation of the redress offer, including:

(a) if there is no loss on the valuation date, a clear explanation of why this is the case; and

(b) if the result is a loss on the valuation date:

(i) the total amount of redress calculated, with the primary compensation sum and the secondary compensation sum shown separately;

(ii) confirmation that if the redress offer is accepted by the *consumer*, the redress paid by the *firm* will be increased to include the additional compensation sum;

(iii) an offer to make payment of redress as a cash lump sum;

(iv) the warning in the form at DISP App 4.3.39R;

(v) if it has not already been requested by the *consumer*, an offer to calculate free of charge the redress that would be payable by full or partial augmentation; and

(vi) an explanation of how the *consumer's* tax position and entitlement to state benefits has been taken into account, including an allowance for any tax charges for which the *consumer* will be liable (and where the *consumer* is responsible for any payment of tax, this should be made clear and a recommendation that they contact HMRC provided).

(3) The terms and conditions of any redress offer, including the following information:

(a) a statement requesting that the *consumer* review the assumptions used in the redress calculation and explaining that they may raise any questions about them with the *firm*;

(b) that the redress offer is valid for a 3-*month* period from the date it is issued to them, during which period the *consumer* can consider their options and the offer will remain open for acceptance;

(c) how to request that the *firm* calculate the redress that would be paid if the *consumer* directs for the redress to be paid by full or partial augmentation;

(d) how to accept or reject the redress offer; and

(e) the process for resolving any *complaints* about the redress calculation or redress offer.

App4.3.39 **R** Where any of the redress is paid in the form of a cash lump sum to the *consumer*, a *firm* must provide:

(1) a warning that this amount, in addition to the pension value in the *consumer's* DC pension arrangement, is intended to provide the *consumer* with the equivalent retirement income they would have received if they had not transferred out of their *defined benefit occupational pension scheme*, but only as long as the *consumer* invests it prudently; and

(2) a warning that if the *consumer* does not invest the redress prudently, they risk losing out on the retirement income their redress amount is meant to provide; and

(3) information about trusted sources of free advice and guidance on making investment decisions and avoiding investment scams, such as Pension Wise, *MoneyHelper* and the *FCA's* 'Scam Smart' guidance; and

(4) an explanation of the risk and consequences of making an unauthorised payment, including the risk of unauthorised payment charges being levied.

App4.3.40 **R** When a *firm* communicates a redress offer to a *consumer*, it should:

(1) take reasonable steps to communicate in a way that is fair, clear and not misleading;

(2) take into account the information needs of the *consumer*, including their understanding of financial services; and

(3) where possible, use plain language and avoid the use of jargon, unfamiliar or technical language.