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| <b><u>Decision Ref:</u></b>             | 2018-0133  |
| <b><u>Sector:</u></b>                   | Investment   |
| <b><u>Product / Service:</u></b>        | Pension  |
| <b><u>Conduct(s) complained of:</u></b> | Failure to provide product/service information<br>Fees & charges applied |
| <b><u>Outcome:</u></b>                  | Partially upheld   |

#### **LEGALLY BINDING DECISION OF THE FINANCIAL SERVICES AND PENSIONS OMBUDSMAN**

#### **Background**

This complaint concerns the Provider's application of a "cash discount factor" to the funds being paid out to him under a pension plan the Complainant took out with the Provider in 1994 and is seeking to claim benefits his from now. This "cash discount factor" has also been referred to as an "early withdrawal penalty".

#### **The Complainant's Case**

The Complainant was a fisherman and was born in 1957. The Complainant took out a pension with the Provider in 1994. In 2016 (approaching his 59<sup>th</sup> birthday) he sought to claim his retirement benefits on foot of the policy.

The Provider has told the Complainant that a cash discount factor is applicable to his benefit claim, in circumstances where he is seeking benefits prior to the retirement age set out under the terms of the policy.

The Complainant states that this was never explained to him when he took out the policy, and that this "early withdrawal penalty" is unreasonable. In addition, he sought specific confirmation on the applicability of an early withdrawal charge in April 2015 and the Provider advised him, in error, that he was entitled to retire from age 55 without an early withdrawal penalty being applied.

The complaint is that the Provider has unreasonably and/or unfairly sought to impose an early withdrawal fee on the redemption of the policy. The Complainant would like to receive his benefits under the pension plan without having to pay the early withdrawal charge.

### **The Provider's Case**

The Provider states that a cash discount factor is applicable if a policyholder retires before 65, pursuant to the terms and conditions of the policy. It has apologised for providing incorrect advice to the Complainant in April 2015 and has offered the sum of €500 as a gesture of goodwill.

### **Decision**

During the investigation of this complaint by this Office, the Provider was requested to supply its written response to the complaint and to supply all relevant documents and information. The Provider responded in writing to the complaint and supplied a number of items in evidence. The Complainant was given the opportunity to see the Provider's response and the evidence supplied by the Provider. A full exchange of documentation and evidence took place between the parties.

In arriving at my Legally Binding Decision I have carefully considered the evidence and submissions put forward by the parties to the complaint.

Having reviewed and considered the submissions made by the parties to this complaint, I am satisfied that the submissions and evidence furnished did not disclose a conflict of fact such as would require the holding of an Oral Hearing to resolve any such conflict. I am also satisfied that the submissions and evidence furnished were sufficient to enable a Legally Binding Decision to be made in this complaint without the necessity for holding an Oral Hearing.

A Preliminary Decision was issued to the parties 25 July 2018, outlining the preliminary determination of this office in relation to the complaint. The parties were advised on that date, that certain limited submissions could then be made within a period of 15 working days, and in the absence of such submissions from either or both of the parties, within that period, a Legally Binding Decision would be issued to the parties, on the same terms as the Preliminary Decision, in order to conclude the matter.

In the absence of additional submissions from the parties, my final determination is set out below.

There is no dispute about the Complainant's entitlement to retirement benefits from the age of 55.

This complaint is therefore two-fold. The first part concerns the fairness or otherwise of the Provider applying a cash discount factor to the policy. The second part concerns incorrect advice given to the Complainant by the Provider in April 2015.

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### **Cash Discount Factor / Early Withdrawal Penalty**

The terms “cash discount factor” and “early withdrawal penalty” were used by both parties to this complaint, and refer to the same thing: the monies to be paid over by an annuitant where they seek to retire and claim benefits under the policy earlier than the retirement age designated by the policy.

The Provider in its final response letter provided a clear explanation of how this charge arises, as follows:

*“When your plan started, the money paid in was used to buy ‘initial units’ which have a higher management charge applied to them then accumulated units and therefore grow at a slower rate. After the period of buying initial units your payment was used to buy accumulated units which have a lower management charge.*

*The initial units purchased continue to be held and continue to have the higher management charge applied to them up to your plans maturity date of 10 August 2022. At this date all initial units are due to be converted to accumulated units and a Cash Discount Factor will cease to be applied.*

*Purchasing initial units is a mechanism for recouping the charges associated with setting up a plan. Charges such as commission, administration costs etc. This initial unit mechanism allowed us to spread the charges evenly over the entire term of your plan from the start date to the maturity date, instead of taking all these charges upfront when your plan started....”*

*“If your plan is claimed before the maturity date we will not have time to fully recoup the costs we incurred over the years. Therefore we apply the early withdrawal penalty (cash discount factor) when calculating the final value of your plan.”*

*“The fact that your plan was written to age 65 meant we had 28 years to recoup these charges. If your plan had been set up to be taken to an earlier age, such as age 60, the period to recoup the charges as outlined above would have been less.”*

In other words, charges applicable under the plan are spread over the lifetime of the plan instead of being payable as one lump sum payment at inception. However, if the Provider has planned to spread the charges over a certain period of time, but an annuitant seeks to end the policy early, the Provider is at a loss. The cash discount factor is not a “penalty”, as such, but is in fact a charge that seeks to recoup (or bring forward) the payments that the Provider would have received incrementally had the policy ran its full term.

The Provider has cited paragraph 25 of the policy terms and conditions which explains the “cash discount factor” as follows:

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*“For the purposes of conditions 11, 22, 23, 24, 28, 49, 50, 59 and 61 Accumulation Units of the Investment Funds are valued at their bid prices, while Initial Units of Investment Funds are valued at their bid prices multiplied by the ‘cash discount factor’. The cash discount factor is equal to 1 successively multiplied by the Monthly Multiplier for each month remaining until the Maturity Date. The Monthly Multiplier shall equal the excess of 1 over the additional monthly rate of charge of Initial Units specified in Table 3 of Schedule 2. The value of Initial Units and Accumulation Units of the Pension Capital Guaranteed Fund will, for the purposes of the said conditions, be determined by the Company.”*

Paragraphs 28 of the policy terms and conditions set out how the Cash Value of the policy will be calculated at a date *“other than Maturity Date while the policy is still in force”*.

The Provider also points to Annual Benefits Statements since 2013 which notes:

*“We will apply an initial units cashing factor charge if you take retirement benefits before your nominated (normal) retirement age or if you transfer your funds to another pension plan.”*

However, the annual statements do not set out what the Complainant’s nominated retirement age is, so if he was under the impression that his nominated retirement age under the policy was 55 the foregoing note would not have provided any warning to him.

The Provider emphasises that the policy would have been written on the basis that the Complainant would not retire until he was 65. It notes that the pension provider at the time would have written to age 65 as standard, and it is not aware of any pension product available in 1994 that would have specifically catered for individuals who were entitled to retire before 60 due to their occupation.

The *“Declaration and Signature”* section of the application form signed by the Complainant on the 26<sup>th</sup> of October 1994 states:

*“I understand that the maturity date of this contract shall be taken as my 65<sup>th</sup> birthday. Where, however, a different cover ceasing age is specified in Section 4 or 5 of this proposal form, then I understand that the maturity date this contract shall be taken as the later of the cover ceasing ages so specified in Section 4 or 5.”*

There is no different cover ceasing age specified in sections 4 of 5 of the proposal form.

Having examined the terms and conditions attaching to the policy, there is no doubt that the Provider is entitled to apply the cash discount factor. There is no basis for me to find that the application of same is unfair or unreasonable – it is provided for in the terms and conditions and is designed to recoup charges and commissions that would otherwise be spread out over the full term of the policy.

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Therefore, I do not uphold this aspect of the complaint.

I do note that (although the Provider was not the author of them) the terms and conditions that attached to this policy would be utterly incomprehensible to anyone without some sort of background in products of this nature. Having said that, for the reasons set out above I am not in a position to make a finding in relation to matters which occurred or the nature of the advice given in 1994.

**Incorrect advice in April 2015**

On the 27<sup>th</sup> of April 2015 the Complainant's financial advisor emailed the Provider in the following terms"

*"I did a call last week with [the Complainant], we reviewed the above policy,*

*He said that this plan was sold to him with the distinct message that because he was a fisherman he would be able to access his funds early.*

*However when I told him there is an early exit penalty of €11372 he said that this was never mentioned to him when he bought the plan.*

*He asked why would a company tell you that you can access your funds early because of your occupation and not mention an early exit penalty of such magnitude?*

*He said he would never have entered into a contract with these types of penalties if he was made aware of them.*

*He said that he felt this was a very serious issue and that he felt this penalty should be foregone by the company..."*

On the 30<sup>th</sup> of April 2015 the Provider emailed the following in reply:

*"I can confirm that as per the attached document, [the Complainant] is entitled to retire after age 55 with no early withdrawal penalty being applied."*

The Provider has stated that this email referred to the "Market Value Adjuster" penalty rather than the cashing in factor charge, and has accepted that *"there may have been some confusion created as a result of the ambiguous response given"*. This is an understatement. The email of the 30<sup>th</sup> of April 2015 would have completely misled the Complainant. It was not an ambiguous response, it was simply incorrect. There was no reasonable basis for the Provider to believe the Complainant's email was inquiring about the Market value Adjuster as opposed to the cash discount factor – even allowing for the differing terminology used ("early exit penalty"), the precise figure of €11,372 was quoted.

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Providing incorrect information of this nature to a person considering and planning for their retirement can have very serious consequences.

However, the error did not alter the terms and conditions, nor did the Complainant act to his detriment on the basis of it. The contract that was entered into in 1994 permitted the Provider to recover its charges/commissions incrementally over the entire term of the policy remained applicable. An error in 2015 does not mean that the Provider is not entitled to the said charges/commissions.

It is also worth noting that the Complainant has not been misled in a truly material fashion, given that his annual statements since 2007 have always set out a net figure (taking the cash discount factor into account) as the current/cash value. This is not a situation where the Complainant was receiving statements misleading him as to the true encashment value.

While I consider the error of April 2015 to be a serious one, I do not consider that disallowing the cash discount factor would be a proportionate response.

On the other hand, I do not consider the Provider's goodwill gesture of €500 to be commensurate with the gravity of its error. In order to do justice between the parties, I partially uphold this complaint and direct the Provider to pay the Complainant a sum of €3,000.

## **Conclusion**

My Decision pursuant to **Section 60(1)** of the **Financial Services and Pensions Ombudsman Act 2017**, is that this complaint is partially upheld on the grounds prescribed in **Section 60(2) (e) and (g)**.

Pursuant to **Section 60(4) and Section 60 (6)** of the **Financial Services and Pensions Ombudsman Act 2017**, I direct the Respondent Provider to make a compensatory payment to the Complainant in the sum of €3,000, to an account of the Complainant's choosing, within a period of 35 days of the nomination of account details by the Complainant to the Provider. I also direct that interest is to be paid by the Provider on the said compensatory payment, at the rate referred to in **Section 22** of the **Courts Act 1981**, if the amount is not paid to the said account, within that period.

The Provider is also required to comply with **Section 60(8)(b)** of the **Financial Services and Pensions Ombudsman Act 2017**.

**The above Decision is legally binding on the parties, subject only to an appeal to the High Court not later than 35 days after the date of notification of this Decision.**

**GER DEERING  
FINANCIAL SERVICES AND PENSIONS OMBUDSMAN**

17 August 2018

Pursuant to **Section 62** of the **Financial Services and Pensions Ombudsman Act 2017**, the Financial Services and Pensions Ombudsman will publish legally binding decisions in relation to complaints concerning financial service providers in such a manner that—

**(a) ensures that—**

- (i) a complainant shall not be identified by name, address or otherwise,**
  - (ii) a provider shall not be identified by name or address,**
- and**

**(b) ensures compliance with the Data Protection Regulation and the Data Protection Act 2018.**