DRN-3043143

The complaint

Ms S complained about the advice she received from Wesleyan Assurance Society to take out a free-standing additional voluntary contribution (FSAVC) plan. She says if she'd been given adequate information during the sale about her options, she would have bought added years in her employer's occupational pension scheme (OPS).

Ms S is being assisted with her complaint by a claims management company (CMC). And both Wesleyan and the CMC have actuaries working with them to resolve this matter. However, for ease of reading the decision, I'll refer to all representations and arguments as being raised by either Wesleyan or Ms S.

What happened

In September 1998, Ms S was advised by Wesleyan to start contributing to an FSAVC plan. At the time, Ms S was a member of her employer's OPS. The FSAVC plan commenced with Ms S making a monthly contribution of £70 (gross). This increased to £100 (gross) from February 2007. The last contribution was paid to the FSAVC plan in February 2016.
In 2002, while still making contributions to the FSAVC plan, Ms S contracted to buy added years through her employer's OPS. This was at a cost of 1.03% of her pensionable pay for each year, payable until age 60. Ms S paid a total of 5.30% to buy 5 years and 53 days, which was the maximum number of added years Ms S was able to purchase, taking her up to the 40 year service limit.

In 2016, Ms S complained to Wesleyan about the sale of the FSAVC plan. In summary, she complained that:

- The FSAVC plan was not suitable for her needs and as a result of being mis-sold, she's suffered a financial loss;

- The full risks, implications, and alternatives in respect of the FSAVC plan were not fully and properly explained. And she wasn't provided with a full or descriptive comparison of benefits between her in-house scheme and the FSAVC plan;

- She was unaware that the FSAVC plan had higher charges and she should've been advised to purchase added years through her employer's scheme.

Wesleyan reviewed the complaint. In its final response it explained that, having considered the sales paperwork and the information Ms S had provided in her FSAVC questionnaire, it wasn't satisfied that Ms S had been given adequate information about the risks and charges of the FSVAC policy. So it was upholding the complaint. And it said that it had forwarded Ms S's file to its actuaries for a loss assessment to be completed on an added years basis. A further letter was issued in February 2017 after the loss assessment had been completed.

The letter confirmed the following:

- Ms S had suffered a financial loss as a result of the advice received to take out the FSAVC plan instead of being a member her OPS 'added years' arrangement from September 1998 to September 2002.
- The calculation had been based on the assumption that Ms S would've bought added years from September 1998, the earliest date possible after receiving advice from Wesleyan, and was based on a retirement age of 60.
- In September 1998, Ms S could've purchased 1 year additional pensionable service at a cost of 0.85% of pensionable pay payable for a term of 25 years to Normal Retirement Age (60). The maximum number of added years she would have been permitted to purchase in 1998 would have been 5 years 53 days. This would have been at a cost of 4.37% over 25 years.
- Between 1998 and 2002 the FSAVC contributions were equivalent to 1.90% of pay. If contributions at this level had been directed to the added years arrangement instead of the FSAVC they would have bought 2 years 86 days if contributions had been paid at this rate until age 60.
- In September 2002 Ms S contracted to buy 5 years 53 days added years in the OPS at a cost of 5.30%.
- Ms S hasn't lost the opportunity to buy the maximum number of added years. However, the delay in contracting to buy them has caused her to pay a 0.40% higher contribution rate for the 2 years 86 days that she could have purchased with her FSAVC contributions.
- The part of the FSAVC policy that is attributable to contributions that were made to the plan between September 1998 and September 2002 is a gain that offsets the loss due to the additional added years contributions Ms S has paid subsequently.
- Assuming that Ms S maintains the added years contract to age 60, her loss (if any) is the value of the additional contributions of 0.40% of pensionable pay that she is paying, since she commenced her added years contract in September 2002, less the value of the added years contributions of 1.90% that she paid instead into the FSAVC contract between September 1998 and September 2002.
- The loss assessment as at 1 July 2016 had determined that:-

The value of the additional contributions paid over the period from September 1998 to 1 July 2016 increased with interest at bank base rate:	**£5,141.00**
The present value of the future additional contributions to be paid from 1 July 2016 to September 2023 (age 60) discounted to a present value on a basis that is consistent with the Financial Ombudsman Service assumptions for the valuation of an earnings-related annuity is:	**£3,529**
The value of the additional contributions is therefore:	**£8,670**
The estimated value of the part of the Plan, net of future charges that Ms S has acquired instead of contributing to Added Years during the period September 1998 to September 2002 is:	**£6,838**
Ms S's net gain at 1 April 2018 is therefore (£8,363.01 - £8,377.29) =	**£1,832**

- Redress offer - Wesleyan proposed to offer redress as a cash sum, adjusted to reflect tax relief at 40%. Interest calculated at Court Rate (8% per annum) less higher rate tax was added for the period from 1 July 2016 to 17 March 2017, resulting in redress of **£1,148.88**

As the matter hadn't been settled before the FCA updated the methodology for calculating redress for unsuitable defined benefit transfers, Wesleyan was required to recalculate the position. In its June 2018 letter, Wesleyan confirmed that as at 1 April 2018:-

The value of the additional contributions paid over the period from September 2002 to 1 April 2018 increased with interest at bank base rate:	**£5,902.10**
The present value of the future additional contributions to be paid from 1 April 2018 to September 2023 (age 60) discounted to a present value on a basis that is consistent with the FOS assumptions for the valuation of an earnings related annuity is:	**£2,460.91**
The value of the additional contributions is therefore:	**£8,363.01**
The estimated value of the part of the Plan, net of future charges that Ms S has acquired instead of contributing to Added Years during the period September 1998 to September 2002 is:	**£8,377.29**
Ms S's net gain at 1 April 2018 is therefore (£8,363.01 - £8,377.29) =	**(£14.27)**

Wesleyan's letter explained that the value of the relevant proportion of the FSAVC plan was higher than the value of the benefits Ms S would have bought in the OPS by a margin of £14.27. As a result, no compensation was due as its calculations showed that Ms S hadn't incurred a financial loss.

Ms S didn't agree with the methodology Wesleyan had used in its loss assessment so she referred the complaint to our service for review. In summary, Ms S has said that Wesleyan's actuaries have used the value of her own contributions in the purchase of added years to further offset the loss caused by the advice to purchase the FSAVC. Ms S says this is not allowed under the FSAVC Guidance. The loss calculation period is clearly set out in guidance and is stated to be:

> ***"The period for loss assessment will end on the earlier of:***
>
> ***1) the 6th April after the investor stopped paying into the FSA VC policy, and***
>
> ***2) the date the investor started paying into the in-house A VC scheme.***
>
> ***Starting to buy added years counts as joining the in-house A VC scheme and so will end the period of loss assessment.***
>
> ***If the investor starts to buy added years but also continues to pay into the FSAVC policy, I believe that the period of loss assessment would end when the investor starts to buy added years (unless the investor can show that the insurer/adviser gave some subsequent advice, e.g. in connection with a subsequent FSA VC premium increment)."***

Ms S believes that the value of the benefit is outside the loss calculation period and should not be applied. This is confirmed both by the FCA and the actuaries Ms S's CMC has instructed. Wesleyan is incorrect to state that the loss is simply the differential in the cost of purchase caused by deferring the start date of the added years. In reality it's effectively deducting the added years purchased.

<u>*My provisional findings*</u>

I reviewed the complaint and issued a provisional decision in February 2022. My provisional findings are set out below.

"*I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint. Before explaining my provisional findings, I'd like to take this opportunity to apologise to both Ms S and Wesleyan for the delay in the complaint being reviewed.*

Wesleyan has upheld the complaint on the basis that the FSAVC plan was mis-sold. And it considers that, had she been given adequate information during the sale, Ms S would've chosen to buy added years in the OPS in 1998, rather than taking out the FSAVC plan. As both Wesleyan and Ms S are in agreement on this matter, my decision focuses on what Wesleyan needs to do to put matters right; I don't intend to comment on the sale of the FSAVC plan and whether I agree that Ms S would've chosen added years in 1998 as these matters no longer seem to be in dispute.

In considering what needs to be done to put matters right, I've taken into account the law, any relevant regulatory rules, guidance and good industry practice.

This service doesn't have the resource to check the actual calculation that is in dispute. Instead, I've considered the calculation methodology Wesleyan has used. Having done this, I'm currently of the view that Wesleyan's calculation methodology is unfair and so I'm minded to uphold the complaint in part. I'll explain why.

<u>*The FSAVC Review Model Guidance and Review Bulletin 3*</u>

Following concerns about mis-selling, the regulator at that time, told businesses to carry out a review of some FSAVC plans sold between 29 April 1988 and 15 August 1999. The main aim was to review the FSAVC plans of consumers who might have lost matching contributions or subsidies that the employer would've paid, had an in-house AVC plan been started instead. The sale of Ms S's plan didn't fall within the review because the OPS didn't match or subsidise payments to its in-house AVC arrangement.

However, when we uphold a consumer's complaint that they should've been advised to take out the in-house AVCs instead of FSAVCs, we do generally tell the business to pay compensation in accordance with the FSAVC review guidance, even if the FSAVC plan didn't fall within the scope of the review.

It should be noted that, in terms of calculating loss, this guidance was predominately focused on consumers that would've joined their employer's in-house defined contribution AVC scheme. The guidance provided limited information for calculating loss for consumers where it had been decided that they would've bought added years. An additional bulletin was issued in January 2001 – FSAVC Review Bulletin 3. In this the regulator said that:

> "*TREATMENT OF POTENTIAL DEFINED BENEFIT CASES*

(…)(Model Guidance, Section 6 – Loss assessment) The response paper to Consultation Paper 27 (published May 2000) explained the use of benchmark indices for simplified redress calculations but recognised that firms should be allowed to use actual performance to establish whether a loss has been suffered. This will avoid redress being paid where no loss has been suffered. (Response Paper 27, paragraph 73).

This principle applies to defined benefit cases as to all others, and firms may test to see if there is any actual or potential financial loss. ('Defined benefit case' means one where the case has failed compliance, or the firm has conceded compliance, and the firm has established that the investor would have chosen the defined benefit option). Firms should:

- *establish the fund value to be used for loss assessment;*
- *consider whether any other firms are involved; and*
- *determine the relevant period for loss assessment in accordance with the Model Guidance*

Then, in assessing whether there is any actual or potential loss, the calculation should mirror that required for the Pensions Review with the exception that the assumption for future annual salary increases should be RPI + 2% (except where firms can demonstrate that this assumption is inappropriate). For details see paragraphs 6.18.5 and 6.18.6. It is not possible to conduct a simplified loss assessment for defined benefit cases. Firms should conduct a full loss assessment, in almost exactly the same way as they would for the Pensions Review. That is, in defined benefit cases firms have the option either:

- *to concede loss; or*
- *to use actual performance in the loss calculation.*

Firms cannot use benchmark indices in the calculation. Where, in defined benefit cases, the loss calculation indicates that there is an actual or prospective financial loss, or the firm concedes loss, firms should proceed either to causation assessment or to redress and settlement"

While acknowledging that the model guidance and subsequent bulletin are useful, I don't believe strictly applying them is appropriate in the particular circumstances of this case.

Ms S's FSAVC plan didn't fall within the initial scope of the review for which the guidance was intended. And the guidance wasn't written to address every potential scenario, particularly those arising over 20 years after the guidance was issued, where action taken to mitigate loss was taken many years before the complaint was made. And crucially, there's nothing in the Dispute Resolution rules (DISP) – the rules in the FCA handbook that set out how complaints are to be dealt with by firms and the ombudsman service – which stipulates that this guidance must be applied to all FSAVC complaints being raised now, that didn't fall within the initial scope of the review.

That's not to say the guidance and bulletin aren't relevant at all; they do still provide a useful guide, particularly when we consider complaints about mis-sold FSAVC cases where it's been determined that the consumer would've joined their employer's in-house defined contribution AVC scheme. However, in this case I consider departing from a strict interpretation of the guidance is necessary in order to provide Ms S with fair compensation.

I think it's important to explain that when a consumer has lost out financially as a result of something the business has done wrong, I'd generally expect the consumer to be put back *into the position they would have been in, had the business not made the error. This is also the case when considering Ms S's complaint.*

The bulletin referenced above states that after establishing the fund value, considering causation and determining the relevant period for loss assessment, the calculation should mirror that required for the Pensions Review. The Pension Review Guidance has been updated since it was initially issued.

The Finalised Guidance issued by the FCA in 2017 and updated in March 2021 – commonly referred to as FG17/9, states that:

> *"Guidance for firms on how to calculate redress for unsuitable defined benefit pension transfers (…)*
>
> *The standard approach to calculating redress*
>
> *2. Where a firm or adviser has failed to give compliant and proper advice, or has committed some other breach of the relevant requirements**, the basic objective of redress is to put the customer, so far as possible, into the position they would have been in if the non-compliant or unsuitable advice had not been given or the breach had not occurred** {my emphasis}"*

So while I've considered the above model guidance and bulletin when thinking about fair compensation, my main focus has been to put Ms S, as far as possible, in the position she would now be in, had she bought added years in 1998 instead of taking out the FSVAC plan; she shouldn't be placed in better position and equally, she shouldn't be worse off.

<u>How many added years should the calculation be based on?</u>

Wesleyan has calculated that Ms S paid the equivalent of 1.90% of her pensionable pay to her FSAVC plan between 1998 and 2002, when she joined the added years arrangement. Instead of taking the FSAVC plan, if Ms S had paid 1.9% of her salary to the added years arrangement instead, this would have secured her 2 years and 86 days added years at a rate of 0.85% per year if she'd maintained payments until age 60.

Ms S is due to receive 5 years and 53 days as a result of the added years she purchased in the OPS. This was the maximum Ms S could have purchased to take her to 40 years' service. So she's not lost the opportunity to buy added years. However, she's paid more (1.03% rather than 0.85% per year) for the 2 years 86 days that she could have purchased instead of starting the FSAVC. In 2018, Wesleyan's calculations showed that between 2002 and 2023 – when Ms S will be 60 – she will pay £8,363.01 more to her added years arrangement than she would have done, had started added years in 1998. I'm satisfied that the methodology Wesleyan has used in this respect is fair.

Ms S has concerns that Wesleyan has used the value of the added years the above excess contributions secured, to offset the loss caused by the advice to purchase the FSAVC. And she says that Wesleyan is incorrect to state that the loss is simply the difference in the cost of purchase caused by deferring the start date of the added years. Ms S says that in reality Wesleyan is effectively deducting the added years purchased.

However, if Wesleyan fails to take account in its calculation of the full added years Ms S bought, it will likely leave her with a benefit equivalent of more than the maximum level of service she could have had. This is a position that Ms S couldn't ever have found herself in, had she taken added years initially. And the fact that Ms S has taken action to mitigate her loss by contracting to buy added years from 2002, needs to be taken into account.

The FSAVC model guidance wasn't written with the intention that it would address every scenario that arises. And for the reasons explained, I don't believe strictly applying the guidance in this case is appropriate, all the added years Ms S purchased need to be factored into the redress correctly.

Ms S believes that Wesleyan's methodology simply calculates the differential in the cost of deferring the purchase of added years. But I don't think this is an unreasonable approach. I'm satisfied that this approach places Ms S in the position she'd be in now but for Wesleyan's error. It's ensuring she hasn't paid more for the 2 years and 86 days her FSAVC contributions between 1998 and 2002 could have secured.

<u>Should the calculation be bought up to date?</u>

I've thought about whether this calculation should be rerun to bring it up to date. It's not unusual for us to do this where a significant time has passed since the calculation was run and the complaint hasn't been settled. Or we may ask a business to pay interest on any loss identified to account for the consumer having been without access to these funds.

In the case of Ms S, although the calculation was run on an added years basis, it was only to determine the difference between the cost of deferring the purchase of added years. The purpose of the calculation wasn't to determine the cost of replacing any added years that Ms S had lost the opportunity to purchase as she's has purchased the maximum and will be receiving this benefit in full from her OPS. So I believe any changes to the FCA assumptions that would have happened since the calculation was completed, in particular the changes in March 2021, regarding CPI index assumptions, are unlikely to have a significant impact on the calculation. So I'm currently minded to say that, because I don't think the methodology Wesleyan has used here is unfair, there is no need for the calculation to be rerun. And as the calculation showed that Ms S had in fact not suffered a loss, there's no need for Wesleyan to make a payment to her in settlement of this aspect of the complaint.

<u>FSAVC contributions between 2002 and 2016</u>

Although, I'm minded to say that Wesleyan doesn't need to take any further action in respect of the added years aspect of this complaint, I'm conscious that it hasn't taken account of the contributions Ms S paid to her FSAVC plan after she joined the added years arrangement in 2002. Ms S continued contributions of £100 per month to her FSAVC plan after she joined the added years arrangement.

Wesleyan acknowledges that it mis-sold the FSAVC plan and that Ms S wasn't given adequate information during the sale. It's satisfied that she would have opted for added years had she been given the correct information. However, had Ms S been made aware she could also contribute to the in house AVC plan – with likely lower charges than the FSAVC - as well as purchasing the maximum number added years, I think it's likely that she would have opted to direct the contributions paid after 2002 to the in-house AVC.

I've not seen any evidence that Ms S wouldn't have had the headroom to make these payments to the in-house AVC. My understanding is that Ms S could have contributed a maximum of 9% of her salary to both in the in-house AVC and added years arrangements. However, I do acknowledge that Wesleyan has previously said, on another case, that when the maximum number of added years is being purchased, the cap for in-house AVC contributions is around 2% or 3%. The information I've seen suggests that Ms S was earning £57,566 in 2002. So her monthly contribution of £100 would have been just over 2% of her salary. So even if the cap was as low as 2 or 3%, I think it's likely Ms S would have had the headroom to direct these additional contributions to the in-house AVC. As such, in my final *decision, I intend to direct Wesleyan to carry out a charges only calculation on the contribution Ms S paid to the FSAVC after 2002.*

Responses to my provisional findings

Wesleyan didn't provide any comments in response to my provisional decision.
Ms S's representative provided further submissions which I've summarised below.

- Wesleyan is using Ms S's own purchase of added years to offset its liability. Ms S's representative does not believe this compensates Ms S fairly and it considers it breaks the guidance issued by the regulator. No other firm adopts this approach and nor has the FSCS. This is a change in approach by Wesleyan as it hasn't always used this methodology. Wesleyan is wrong to say that the use of Ms S's own purchase of added years, even if this is "outside of the loss calculation period", can be taken into account as "*a client cannot be compensated to a higher degree than they would have been in, had they purchased added years from outset*". Ms S completely agrees that a client cannot and should not be over-compensated, but this is not the case.
- There are two sets of contributions to the pensions – the FSAVC and the added years contributions, however, Wesleyan's methodology shows zero difference in outcome. This is clearly wrong and Wesleyan should not deduct the value of the FSAVC, and so its loss is understated. It appears that, *for benefits*, Wesleyan is modelling the 'Notional Scenario' against the 'Actual Scenario'. However, *for contributions*, it's modelling the same 'Notional Scenario' to added years, but against the 'Actual Scenario'. Consequently, the difference in *benefits* is the value of the FSAVC, but the difference in *contributions* is actually *higher* than Wesleyan calculates so its loss is understated.
- Wesleyan is mis-using the information to manipulate a no loss scenario – and the most obvious error is the deduction of the value of the FSAVC to produce the zero difference in output.
- The calculations only include the higher cost of buying 2 years and 86 days added years, from 2002 instead of 1998, not the higher cost of all the added years being bought (5 years 53 days). So Ms S still needs to be compensated for the higher cost of the additional added years.
- If it is decided to restrict the added years to the number that Ms S would've bought from 1998, to the number of added years purchased from paying 1.9% contributions, then the number of added years should also be restricted to what 1.9% contributions could have bought from 2002. From 2002, 1.9% contributions would only have bought 1 year 308 days of added years, not the 2 years 86 days that paying 1.9% from 1998 would have bought. So the calculations should then include the (benefit) value of the missing 143 days of added years (2 years 86 days – 1 year 308 days), which it does not currently include.

My side letter to both parties updating redress

After reviewing the responses to my provisional decision, I issued a further letter to both parties explaining that I was minded to make a change to the redress. I also clarified why I wasn't asking Wesleyan to calculate the benefit value that Ms S considers should be included in the calculation. The content of my letter is set out below.

"I think it's important to explain that while I have taken account of the FSAVC review guidance, I don't believe that it's useful in this case when trying to put Ms S back in the position she would be in now if she had taken added years in 1998.

I acknowledge what the FCA has said about the period for loss assessment, which is set out in the FSAVC review guidance. But I would also highlight that it has said that it doesn't get involved in individual disputes; that's a matter for the Financial Ombudsman Service if things can't be resolved between the parties involved.

There is nothing in the Financial Ombudsman Service's rules that states that the FSAVC review guidance must be applied to all complaints that are upheld regarding mis-sold FSVAC plans.

Our rules state that I must award fair redress and in order to that in this case, I consider departing from the above guidance is appropriate.

I also note what Ms S has said about the methodology used by the FSCS. However, the FSCS and our service operate under a different set of rules. The FSCS's rules stipulate that the guidance must be applied, unless it considers departing from it is appropriate in the circumstances of the complaint. However, no corresponding rule exists for the Financial Ombudsman Service. I also think it's important to note that the FSCS would need to consider the relevant time limits and the merits of the complaint, before considering what redress, if any, is due. And even in those circumstances, the FSCS can depart from the FSAVC guidance if they feel it's necessary in order to provide fair redress.

I think what I'm proposing below, puts Ms S in the position she would be in now, if she hadn't taken the FSAVC plan out and instead had bought added years in 1998.

<u>How many added years should the calculation be based on?</u>

At the moment, Wesleyan has calculated that Ms S paid the equivalent of 1.90% of her pensionable pay to her FSAVC plan between 1998 and 2002, when she joined the added years arrangement. It's calculated that this would have secured her 2 years and 86 days added years, at a rate of 0.85% per year, if she'd started added years in 1998 and maintained payments until age 60.

When Ms S started her FSAVC plan, she contributed £70 pm. Based on the information set out in Wesleyan's calculation, it looks like Ms S was earning £26,481.80 that this time. So £70 pm, would have been around 3.17% of her salary. At the rate of 0.85% per added years, this would have secured over three and half years added years at the point of sale.

Had Ms S joined the added years arrangement in 1998 as opposed to taking out the FSAVC plan, this £70 pm would have increased in line with any changes to Ms S's salary as contributions would have needed to be maintained at 3.17% to secure the added years. Both parties are in agreement that Ms S would have bought added years so it follows that she would have been prepared for her contributions to increase above the initial £70pm. This is more than the 1.9% of salary that Wesleyan has based its calculation on. So to ensure Ms S is put back in the position she would have been in, had the FSAVC plan not been taken out, I believe the calculation needs to be rerun on the basis of the number of years the initial £70pm contribution could have secured.

I can understand why Wesleyan has used the 1.9% as this does reflect what Ms S paid to the FSAVC plan between 1998 and 2002. And basing its calculation on this higher initial number of added years, as I've proposed above, will mean that there is a contribution shortfall. Ms S will have paid less to her FSAVC than she would have paid to the added *years arrangement between 1998 and 2002. So the value of the contribution shortfall will need to be factored in to the calculation. But in turn this will also mean that Ms S will have paid more between 2002 and when she retires for approx.3.5 years rather than 2y 86 days. So the calculation will also need to determine how much extra she has paid since 2002.*

Should the calculation be rerun?

Although I was previously of the view that it wasn't necessary for the calculation to be rerun, as there has now been a slight change to the number of added years Ms S would have purchased at the point of sale, in my final decision I intend to direct Wesleyan to rerun on the basis I've set out above.

And for the reasons explained in my provisional decision, I intend to direct Wesleyan to carry out a charges only calculation on the contribution Ms S paid to the FSAVC after 2002.

Value of benefits

Ms S still maintains that Wesleyan is using the value of the added years benefit she secured to offset its liability.

Although above I've suggested the calculation is rerun using the number of added years the initial £70 pm contribution would have secured, to avoid confusion when addressing the 'value of benefits' issue, I think it makes sense to refer to the 1.9% contribution rate, which would have secured 2 years 86 days in 1998 as this is what was set out in my provisional decision and it's on this basis that Ms S has presented her counter argument.

I accept that in 2002 when Ms S started to purchase added years, 1.9% would have secured less added years than in 1998 because the cost of each year had increased. Ms S believes this difference to be 143 days (2y 86 days – 1y 308 days). And she considers Wesleyan is using the added years she purchased to offset its liability.

I've acknowledged in previous correspondence that different actuaries will have their own method of determining what they considered to be correct redress and some of these may be more generous than others. And I accept that the value of this 143 day benefit is greater than the contributions made to purchase it. But Ms S hasn't lost this benefit. She will still receive her full added years entitlement from her OPS.

So while Ms S's actuary may have dealt with these added years differently, I don't think Wesleyan is being unfair. I'm satisfied that if Wesleyan completes the calculation as I've set out above, it will be placing Ms S in the position she would have been in, had she bought added years in 1998. She will receive 5y 53 days added years benefits from her OPS scheme, and she won't have paid any more for the number of years her initial £70pm contribution could have secured.

Ms S has concerns because she says the calculation only considers the cost of buying the added years, it takes no account of the value of the benefit provided by the added years. But in this case, where a member has secured the full added years they were entitled to, albeit at an increased cost, no benefit has been lost and so I'm not going to be asking Wesleyan do any more in this regard. And contrary to what Ms S has suggested, in this case, the value of the FSVAC plan is not being used to replace any added years. There are no lost added years as Ms S will receive her full entitlement from the scheme.

Ms S also says that the value of the FSAVC should not be deducted as this understates the loss. But I don't agree.

The value of the plan (in respect of the proportion representing contributions paid between 1998 and 2002) needs to be taken into account in order to put Ms S back in the position she would have been in. Any value in excess of the contributions paid during this period is a gain and it's not unreasonable for Wesleyan to use this gain to offset against any loss Ms S may have suffered as a result of the extra she has paid to secure the added years.

If Ms S is redressed as I've set out above, she will receive the full added years entitlement from her OPS and she won't have paid any more for the years her initial contribution would have secured. This puts her back in the position she would have been in had she not taken the FSAVC plan out and had instead started the added years contract in 1998 If she also received the value of any investment gain made on the FSAVC contributions, she'd be a in better position."

Ms S's final submissions

Ms S's representative is concerned as the redress proposed "requires" that the existing added years contract is continued up to age 60. If the contract ends before, because Ms S leaves NHS employment or she just decides to stop it, then the number of added years actually bought will be less than if Ms S had started buying the added years in 1998. Currently, Ms S has paid around 19.46 years of the required 21 year term and so has only purchased 92.7% of the 3 years 266 days added years. If Ms S had started in 1998, then by now she would have paid for 23.46 years of the required 25 year term, or 93.9% of the 3 years 266 days added years. So she has currently accrued 16 days fewer added years than she would have done by now if she had started in 1998.

At the moment the redress is suggesting that Ms S would have paid 3.17% from 1998 for 25 years to buy 3 years 266 day of added years; and also 1.46% from 2002 for 21 years to buy 1 year 152 days of added years. Whereas she is actually paying 5.30% from 2002 for 21 years to buy 5 years 53 days of added years. This is equivalent to comparing:

- (Notionally) paying 3.17% from 1998 for 25 years to buy 3 year 266 day of added years; against
- (Actually) paying 3.84% from 2002 for 21 years to buy 3 years 266 days of added years.

Wesleyan's final submissions

Wesleyan understands that it's being asked to rerun the calculation of "difference in cost" to allow for a notional scenario in which Ms S would have contracted to purchase circa 3.5 "Notional" added years from September 1998 rather than the 2 years 86 days which it has used in its calculation.

The 3.5 years added years has been determined by considering the initial FSAVC contribution and comparing this to Ms S's earnings in the tax year commencing 1 April 1998. But Wesleyan has explained that Ms S had service break between March 1998 and August 1998. As such her gross earnings over the 1998/99 tax year aren't a good representation of her salary as they only cover 8 months. Wesleyan has provided evidence to support this break in service. And because of this break, it believes Ms S's salary was closer to £39,722.70 at the time of advice. This means the starting contribution represents around 2.11% of her salary.

Wesleyan believes that adjusting its calculation from 1.9% to 2.11% would have little impact on the loss calculation but would however introduce complexity into the calculation because as noted there would be a contribution shortfall to value.

Furthermore, calculating the notional added years in the way suggested would not be consistent with the way that Wesleyan has calculated loss for other investors. Whilst it understands the proposal is specific to a scenario where an investor has subsequently entered into an added years arrangement, Wesleyan has a strong preference to use the same calculation methodology on all cases.

The FSAVC model review guidance does not provide any instruction as to how the notional added years should be determined and it is therefore necessary to use a sensible and reasonable method.

Wesleyan is strongly of the view that calculating the notional added years based on the total contribution paid over the term of the FSAVC is appropriate. It considers that using the starting FSAVC rate could result in unfair and unintuitive outcomes. In particular, redress could be higher for an investor who has paid less to their FSAVC overall (but have paid flat contributions), than for someone who has paid more (but started on a lower rate and raised it gradually over time). As such Wesleyan considers that its methodology is more robust and fair between investors.

Wesleyan appreciates that other firms may take a different view on the way that the notional added years are calculated. However, it's very uncomfortable with moving away from its long standing calculation approach. Therefore, from both a practical and consistency perspective, Wesleyan would strongly prefer not to rework the calculation as it has been suggested.

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.

Having reviewed the case afresh and considered the further submissions provided by both parties, I'm partially upholding this complaint. I've explained why below.

<u>FSAVC contributions between 2002 and 2016</u>

I explained in my provisional decision why I was minded to ask Wesleyan to complete a charges only calculation on the contributions Ms S paid to her FSAVC plan after she joined the added years arrangement in 2002.

Neither party provided any comments in relation to this aspect of my provisional decision so I see no reason to depart from my findings in this regard. Therefore, if Ms S accepts my final decision, Wesleyan should carry out a charges only calculation on the FSAVC contributions Ms S paid between 2002 and 2016.

<u>How many added years should the calculation be based on?</u>

In terms of the added years calculation, I remain of the view that the redress should be as set out in my most recent side letter.

Wesleyan has Ms S's salary for the 1998/99 tax year would have been more on the region of £39,722.70. And I note it was recorded on the fact find completed during the sale of the plan that her salary was £39,301.

I think the salary noted in the fact find, which it says is applicable from 1 August 1998, is likely to be the most accurate. So Ms S's starting contribution of £70 per month represented around 2.13% of her salary, slightly more than the 2.11% Wesleyan has suggested. I appreciate 2.13% is lower than the 3.17% I set out in my side letter. So Ms S wouldn't have secured as many years on this initial contribution as I first thought. I do, however, still believe that the calculation should be rerun on the basis of how many added years this initial contribution would have secured. I say this because this does still mean that Ms S would have bought more added years at the start than Wesleyan based its initial calculation on. So she may have suffered an additional loss here and I'm of the view that this method of calculation provides fair redress. And a calculation on this basis would be consistent with how Wesleyan has been directed to complete calculations on other complaints with similar circumstances that this service has seen.

It may not be consistent with the way Wesleyan has calculated loss for other investors in the past. But when Wesleyan upholds a complaint on the basis that the consumer would have bought added years, it follows that must be satisfied that the consumer would have been prepared for their contributions to mirror any changes to their salary as this is what would have happened if they had bought added years. While I'm only making a finding specific to Ms S's complaint, I see no reason why this approach should be different for a consumer that doesn't then go on to buy added years.

I accept that this could result in investors that opt to pay a flat rate of contributions receiving more redress, than if they had paid less initially and increased contributions gradually throughout the duration of the plan. But if an investor had joined the added years arrangement, the number of added years secured would have been set at the outset of the contract. And so I consider this approach more accurately reflects the position the investor would have found themselves in, had they taken added years rather than an FSAVC.

I think it's important to highlight that whether a consumer choses to increase contributions, or not, is a factor that could impact the merits of a complaint in terms of whether it is ultimately upheld on an added years basis or a charges only basis. This is because, as I've said above, to uphold on an added years basis would suggest that Wesleyan is satisfied the consumer would have been prepared to increase their contributions in line with their salary.

<u>Value of benefit</u>

I appreciate that Ms S's representative doesn't agree but I remain of the view that Wesleyan only needs to calculate the difference in the cost of buying added years; I don't believe it needs to calculate the value of the benefit Mr S's excess contributions to the added years arrangement could have secured. I don't intend to repeat my reasons for reaching this decision here as they are clearly set out in both my provisional decision and side letter.

In its most recent submissions, Ms S's representative has argued that if Ms S stopped her added years contract now - because she left NHS employment or she simply wanted to stop paying for added years - then she would have accrued around 16 days less than if she'd started buying added years in 1998.

I agree that this may well be the case. But it's not been suggested that Ms S intends to stop paying for added years before the contract is due to end. And so, on balance, I think it's likely that Ms S will continue her added years contract until the age of 60 and she will receive the full 5 years 53 days added years she contracted to buy. So, if I was to ask Wesleyan to provide redress on the basis that Ms S has currently secured less added years, and Ms S continues with her added years contract as I believe is most likely, this will effectively leave Ms S with a benefit equivalent of 16 days more than 5 years 53 days she was entitled to buy under the added years arrangement. So for this reason, I won't be asking Wesleyan to factor this benefit value into its calculations.

Putting things right

In assessing what would be fair compensation, I consider that my aim should be to put Ms S as close to the position she would probably be in if she had purchased added years in 1998 rather than taking out the FSAVC plan.

Calculation in respect of added years

In order to determine how much extra Ms S has paid as a result of the delay in purchasing added years, Wesleyan should rerun its calculation on the basis of the number of years the initial monthly contribution of £70 could have secured Ms S in 1998. Wesleyan will need to take account of any shortfall in the contributions Ms S paid to her FSAVC plan between 1998 and 2002.

Any loss identified should be adjusted to reflect tax that Ms S is expected to pay in retirement.

FSAVC contributions 2002 and 2016

Wesleyan should undertake a redress calculation in accordance with the regulator's FSAVC review guidance, incorporating the amendment below to take into account that data for the CAPS 'mixed with property' index isn't available for periods after 1 January 2005.

The FSAVC review guidance wasn't intended to compensate consumers for losses arising solely from poor investment returns in the FSAVC funds, which is why a benchmark index is used to calculate the difference in charges and (if applicable) any loss of employer matching contributions or subsidised benefits.

In our view the FTSE UK Private Investor Growth Total Return Index provides the closest correlation to the CAPS 'mixed with property' index. So where the calculation requires ongoing charges in an investment-based FSAVC and AVC to be compared after 1 January 2005, Wesleyan should use the CAPS 'mixed with property' index up to 1 January 2005 and the FTSE UK Private Investor Growth Total Return Index thereafter.

If the calculation demonstrates a loss, the compensation amount should if possible be paid into Ms S's 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 Ms S as a lump sum after making a notional deduction to allow for income tax that would otherwise have been paid in retirement. 25% of the loss would be tax-free and 75% would have been taxed according to her likely income tax rate in retirement – presumed to be 40%. So making a notional deduction of 30% overall from the loss adequately reflects this.

Wesleyan should complete the above calculations as at the date of my final decision. And it should pay 8% simple per year from the date of the final decision to the date of settlement if the matter is not settled within 28 days of the it being notified of Ms S's acceptance.

My final decision

For the reasons explained, I partially uphold this complaint and I direct Wesleyan Assurance Society to calculation redress as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms S to accept or reject my decision before 28 April 2022.

Lorna Goulding
Ombudsman