DRN-3418480

The complaint

Mr and Mrs W's complaint is about a mortgage endowment policy they were sold in 1987 over a term of 21 years. They have said that the policy was mis-sold as they were first-time buyers with no investment experience and were financially inexperienced. They said that they didn't understand the policy. They also said that the option of a repayment mortgage wasn't discussed. The policy was originally sold by Abbey Life Assurance Company, but Phoenix Life Limited is now responsible for the sale.

Mr and Mrs W are represented by a claims management company (CMC).

What happened

In 1987 Mr and Mrs W were sold a low start, low cost mortgage endowment policy. This meant that the premium started low and increased by 20% of that figure each year for the first five years. The target value and life cover were set at £24,000 and the term was 21 years. The policy was invested in a mixture of funds: 25% Equity Fund, 25% American Fund and 50% Managed Fund.

The application form recorded Mr W as an assistant chief storekeeper and Mrs W as an assembly line operator. Mr W was 38 years old and Mrs W was 34 years old.

Mr and Mrs W also filled in a mortgage endowment questionnaire for this service. They confirmed that in 1987 they were planning on retiring at 65 and 60 years old respectively. Their joint income was around £20,000 and they one dependent child.

The last policy premium was paid in February 1999 and the policy was then made paid-up. This meant that the unit holding remained invested, but the life cover was reduced to the value of the policy unit-holding. In August 2000 Mr and Mrs W surrendered the policy. They confirmed to our investigator that this was due to financial difficulties.

In 2021 Mr and Mrs W complained about the sale of the policy via their CMC.

Phoenix responded to the complaint. It explained that the policy had been taken out before regulation and so the adviser was only obliged to ensure that the recommendation was appropriate for Mr and Mrs W's needs and circumstances. It confirmed that the adviser had not only arranged the endowment policy, but had also arranged the mortgage for Mr and Mrs W, although he was not doing the latter on behalf of Phoenix. It explained that in 2000 Mr and Mrs W had been sent projected maturity values for the policy, based on no further premiums being paid. As this showed that the policy would not achieve its target maturity value, Phoenix considered that Mr and Mrs W would have known they had cause for complaint at that time and so the complaint had been raised too late. It, therefore, didn't investigate the merits of Mr and Mrs W's complaint.

The CMC referred the complaint to this service on Mr and Mrs W's behalf. It didn't agree that the complaint was time-barred.

An Ombudsman colleagues considered Phoenix's opinion about the complaint being time-barred. She concluded that the complaint was one that we could consider the merits of.

One of our investigators then considered the merits of the complaint, but she didn't recommend that it be upheld.

Mr and Mrs W's CMC confirmed that they didn't accept the investigator's conclusions. It didn't consider that the risk associated with the policy was suitable for Mr and Mrs W, given their lack of experience in financial matters. It said that if our investigator couldn't change her conclusions, the complaint should be referred to an ombudsman.

I issued a provisional decision on 23 March 2022, which set out my conclusions and reasons for reaching them. Below is an excerpt.

'*As Phoenix explained to Mr and Mrs W in its final response letter, their policy was taken out before either the investment or mortgage industries were regulated. This means that when we consider such sales, we look at whether the policy appears to be appropriate for the complainant's needs and circumstances. This is a lower level of requirement than that introduced a year after the sale of their policy, when a product had to be suitable. The regulation also brought in the need to document a fact-finding process, in which a consumer's circumstances, needs and attitudes would be explored. This means that, other than the application form, there is no contemporaneous documentation from the time.*

In this case Mr and Mrs W do appear to have been financially inexperienced, in that they didn't have any existing investments or protection policies. They were taking a mortgage that was only slightly more than their joint annual income, which would indicate that they had some flexibility in their ability to pay for any shortfall if one was predicted. In addition, the policy was due to mature around five years before either of their expected retirement ages, so they would have the capacity to deal with any shortfall before they retired. All of which says that Mr and Mrs W were probably in a position to take a risk with the repayment of their mortgage.

This leads me, therefore, to an assessment of the policy they were sold. Whether Mr and Mrs W were in a position to accept a risk with their mortgage repayment or not, the level of the risk associated with the policy would affect whether it was an appropriate fit for their circumstances.

The policy was invested over three unit-linked funds – Managed, American and Equity. The policy would, generally, have been considered to represent an above medium or balanced level of risk due to the fund choices. I then have to consider the specific details of the policy itself.

This was a policy with a slightly shorter than average term, which meant that it would have less time to grow and less chance to recover if there were any drops in the markets that affected its value. In addition, the policy was a low-start arrangement, with the premium increasing over the first five years of the policy. This means that again, the time the policy had to grow was more limited that a standard level premium policy. These factors would slightly increase the risk the policy represented.

When the details of the policy and the funds selected for its investment are combined, I am satisfied that the policy Mr and Mrs W were sold in 1987 would have been considered to represent an above medium level of risk. While Mr and Mrs W may have been in a position to accept some risk with their mortgage, I am not persuaded that a policy with that level of risk was appropriate for first-time buyers with no investment experience.'

Both parties accepted my provisional decision.

What I've decided – and why

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

As both parties have accepted my conclusions, I see no reason to change them. I remain satisfied that the policy sold to Mr and Mrs W was not appropriate for them.

Putting things right

When deciding on the appropriate redress when upholding a complaint, we aim to place the complainants back into the same financial position they would have been in but for the mistake, or as close as possible.

To do so, Phoenix should calculate whether Mr and Mrs W suffered a loss due to being recommended the mortgage endowment policy in 1987. The redress should follow the regulator's guidance, known as RU89. This will compare the position of Mr and Mrs W's mortgage when the endowment policy effectively ceased to be their repayment vehicle – the end of the month the last premium paid covered - with the hypothetical position they would have been in, had they had a repayment mortgage from the outset.

Mr and Mrs W appear to be unsure about who their lender was in 1987. In the situation where a consumer can't remember who their lender was, it is normal industry practice to use Halifax interest rates in the calculation. So unless Phoenix has some records that confirms which lender provided the mortgage to Mr and Mrs W, it should use Halifax rates in the calculation.

Mr and Mrs W kept the policy for a short period after they stopped paying the premiums. As the policy ceased to be active when it was made paid-up, I consider the surrender value as at the date it was made paid-up is the appropriate figure to use in the calculations. The information from Phoenix indicates that this was likely £8,689. If that is incorrect, Phoenix should confirm what the correct value is in response to this provisional decision.

If a loss is identified, Phoenix should pay that sum to Mr and Mrs W. In addition, interest* at 8% per year should be added to the loss from the date of the calculation to the date of settlement.

*If Phoenix considers it is required by HMRC to deduct income tax from any interest paid, it should provide Mr and Mrs W with evidence of the deduction, which they can use for HMRC purposes if required.

My final decision

My decision is that uphold this complaint. I require Phoenix Life Limited to settle the complaint as detailed in 'putting things right' above. Under the rules of the Financial Ombudsman Service, I am required to ask Mr and Mrs W to accept or reject my decision before 4 May 2022.

Derry Baxter
Ombudsman