DRN-3487938

The complaint

Ms C has complained about advice she received from Wesleyan Financial Services Limited (Wesleyan) to take out a Free Standing Additional Voluntary Contribution (FSAVC) plan. She says that she should've been advised to contribute to her employer's scheme instead.

What happened

Ms C met with an adviser from a firm called BMA Services Limited (now the responsibility of Wesleyan) in 1993 and received advice to start a FSAVC plan. The available paperwork from the time of the sale notes that Ms C was 27 years old, single, working and earning £30,000 per year.

The adviser from BMA was independent, this meant that they could advise on products from the whole of the market. The adviser's letter that was issued after the meeting set out the advice. In summary it said:

- The necessary forms had been received so Ms C could cash in her savings plan. This would mean the contributions of £70 to the savings plan would finish.
- Ms C had confirmed that she had rejoined her employer's occupational pension scheme (OPS) with effect from 1 November 1993. She was making contributions of 6% of her salary towards the scheme, which was around £75 per month, reducing Ms C's national insurance by around £30 per month.
- Overall, Ms C would make a total saving of £175 per month
- Ms C had said that she was willing to invest around £50 per month net towards enhancing her retirement benefits. A problem of missing years of service within her employer's OPS had been exacerbated by her decision to take a personal pension.
- The adviser recommended that Ms C take an FSAVC plan, which should be invested in a with profits fund.

Ms C accepted the adviser's recommendation and the FSAVC plan started in late November 1993. It was set up with a normal retirement age of 60 and with net monthly contributions of £50. The payments to the FSAVC continued at the same amount until October 2018.

In November 2018, Ms C complained to Wesleyan about the advice she had been given. Wesleyan upheld the complaint on the basis that it hadn't been able to evidence that Ms C had been told about her in-house options. And it thought the correct advice would have been for Ms C to have contributed to the in-house scheme. It said that it was passing Ms C's file to its actuaries for a loss assessment to be completed on an added years basis.

In July 2019, Wesleyan wrote out to Ms C again to confirm that the loss assessment had been completed. It had determined that she had suffered a loss of £4,199.89, which had been reduced to £2,939.32 when adjusted for the tax that Ms C was likely to pay in retirement.

Ms C was unhappy with the offer, so she referred her complaint to our service. In summary she said that Wesleyan has stated several factual inaccuracies in the offer letter and there is a deliberate attempt to minimise the value of the offer. She said that had she bought added years she could have continued with them even when taking the choice exercise in her employers OPS. And she said she had stopped paying into the FSAVC in 2018 on the advice of a BMA financial advisor, but had she bought added years these would have continued. She also said that Wesleyan had deliberately not used the in-house AVC in its calculations as this would have resulted in higher financial compensation. Ms C said that the in-house AVC is a much closer comparator to the FSAVC.

One of our investigators reviewed the offer Wesleyan had made. She explained that it wasn't her role to check the calculation that had been carried out by Wesleyan's actuaries. But having checked the data input report, the calculation had been based on the pension review methodology and the investigator was satisfied the correct information had been used. So, she didn't think Wesleyan needed to do any more than it had already offered.

Ms C didn't agree with the investigator. She said that she'd had the offer assessed by an independent financial adviser and they had said it was too low. And Ms C maintained that a comparison should be made with the in-house AVC (money purchase) as she was paying into a FSAVC and she said she would have paid into her employer's in-house money purchase AVC.

Our investigator reviewed Ms C's new comments and sought clarification as to what Ms C would have done if she'd been suitability advised as she had mentioned both added years and the in-house money purchase AVC in her correspondence. Ms C said that it's difficult to say whether she would have purchased added years or joined the in-house AVC scheme, as that offer was never made to her. So she would have asked the financial adviser at the time, which scheme was likely to be most beneficial to her and selected the one they recommended on providing the highest yield at pension age.

The investigator reviewed the complaint again and based on the paperwork that was available, she concluded that Ms C would have most likely joined the in house AVC arrangement. She said this because, having reviewed the adviser's letter again, it indicated Ms C had surrendered her savings Plan, possibly to generate more income. It also showed that she was willing to contribute £50 (£66.67 with tax relief) towards her pension at the time.

Given that she wanted to contribute a specific amount and had surrendered her savings, the investigator didn't think Ms C would've been prepared to tie herself into an added years contract, where a percentage of her salary would be deducted, therefore paying more contributions with salary increases.

Ms C didn't agree. She said the investigator has made several speculative comments, in terms of the saving plan being surrendered and the assumption that Ms C would have joined the in-house money purchase AVC arrangement. Ms C has said that the FSAVC plan had high charges (to cover the salesman's commission and cost of administration) which had impacted on the performance and lowered the policy value. In contrast, the AVC options available through her employer were free of charge. As her OPS was a final salary scheme, Ms C says she could have bought extra years of service to boost her pension. The added years arrangement would not have been subject to risky stock market movements, and thus would have likely produced much higher pensions than the FSAVC.

The complaint has been passed to me to decide.

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 the sale of this plan was conducted by an independent financial adviser, they should have explicitly compared what the in-house options (both added years and the AVC) and what the FSAVC had to offer. There's no evidence that Wesleyan did this in the case of Ms C and so the complaint has been upheld.

It's not in dispute that a failing occurred during the advice process. So my decision focuses on what I think would most likely have happened, had that failing not occurred.

Wesleyan thought that Ms C would have bought added years in her employer's OPS. Ms C has mentioned both added years and the money purchase AVC in her correspondence. And although she has said most recently that she would have chosen added years, she has also said that she would have gone with what the adviser recommended as being most appropriate for her and what was likely to achieve the highest yield.

I acknowledge that with hindsight Ms C might have been better off if she'd purchased added years as investment returns have failed to live up to expectations. But I can't safely say she would've taken added years in 1993.

I do acknowledge that Ms C thought that some of the statements made by the investigator were speculative. But it's not appropriate to look at how the in-house options have performed and chose the option that would now place Ms C in a better position. I have to base my decision on what I think Ms C would have done in 1993, had she been given suitable advice. And where there is only limited evidence from the time of the sale, I need to think about what is more likely to have happened on the balance of probabilities.

Ms C started her FSAVC when she was 27 when it appears she had only recently re-joined her employer's OPS. At that time she had a retirement age in the scheme of 60. So it seems likely she would've needed around eight extra years to achieve the full 40 years' service by her normal retirement age.

Ms C has said that the cost of administering added years was free of charge. But I think what needs to be clarified here is that the cost of purchasing added years was not intentionally subsidised by the employer (unlike the main pension scheme). This meant that added years were generally seen as expensive. The pension scheme's actuaries worked out a table of contribution rates which are likely to have involved cautious assumptions about future investment returns – so that the employer did not have to bear an excessive share of providing the benefits. And the cost of added years would've increased with Ms C's salary.

I think, on balance, the evidence suggests Ms C may not have been willing to commit to an increasing contribution at the time of advice. I say this because the adviser's recommendation letter addresses the savings that Ms C will be making by implementing the changes suggested. These savings were important enough at that time for the adviser to set these out in his letter. This suggests to me that making these savings was one of Ms C's objectives at the meeting. And I'm conscious that the letter explained that the missing years of service had been exacerbated by Ms C having previously taken a personal pension. However, rather than using the full saving the adviser had managed to secure for Ms C, she only committed to a £50 net per month contribution, despite there being surplus in the savings the adviser had made. This suggests to me that Ms C was unwilling to pay more than this to her pension arrangement at that time, despite the additional saving she would be making by cancelling her savings plan.

I think it's also important to note that Ms C was single at the time of advice. And part of the contribution she would have paid for added years, had she opted to take these, would have gone towards providing a spouses' pension, which doesn't appear to have been something that Ms C would have required at that time. And when viewed in the investment climate of 1993, a potentially more cost-effective option, albeit involving some minimal risk, was for Ms C to contribute towards a scheme which provided a pension for her only.

Ms C has recently said that she would have likely gone with the scheme that would have provided her with the highest yield. I can see from the illustration of retirement benefits that was issued in 1993, that if Ms C continued to make contributions at the same rate of £50 per month until her normal retirement date of 60, she was guaranteed to receive a minimum pension of £3,056.69 per annum. However, using the regulator's assumed rates of return at that time, which were 6% and 12%, Ms C was expected to get a pension of £4,730 (6%) and £24,300 (12%) per annum. So even in the middle of these regulatory growth rates, the pension could have been several thousand pounds a year even with contributions remaining level. This would have compared favourably to what Ms C might get from making increasing contributions towards several added years, based on her projected salary at retirement.

So I think, had Ms C been suitably advised, she would have chosen to join the in-house money purchase option through her employer's OPS. This is because the adviser ought to have factored in that the added years option was (reasonably) projected to take more from Ms C disposable income than the money purchase AVC, for a comparable level of benefit. And given what I've said above, I'm not satisfied that Ms C would have wanted to pay more towards her pension.

As I've said above, it's mainly with hindsight that it can be seen that choosing to purchase added years in the 1990s would have resulted in a much better pension now than a 'money purchase' scheme. Unfortunately, the hoped for growth rates haven't been reached - far from it. This is not unique to Ms C's plan, investments across the board haven't performed as expected. Across the industry most investment classes have had problems. The economic and regulatory situation is very different now from what it was in the 1990 when the policy was sold.

I appreciate that had Ms C taken added years, she would not have been impacted by the wider investment climate but for the reasons I've explained above, I'm not satisfied that she would have opted for added years if she'd been suitably advised at the time of the sale. I uphold this complaint on the basis that Ms C would have opted to contribute to her employer's in-house AVC scheme.

The in-house scheme would likely have had lower charges than the FSAVC. But just because Ms C would have paid less in charges, it doesn't necessarily mean that she has suffered a loss as a result of taking the FSAVC. Wesleyan has raised this issue on other cases as it considers its FSAVC funds have performed particularly well.

The regulator's FSAVC review guidance allows a firm to consider if no loss has been suffered and one of the instances where it can do so "*is where the investment performance of the FSAVC has exceeded that of the in-house AVC arrangement by more than the cumulative value of the lost employer contributions and any difference in charges.*" So, I'm directing Wesleyan to carry out a comparison between the FSAVC and the in-house AVC. If it can demonstrate that the FSAVC's performance has exceeded the in-house AVC by more than the higher charges Ms C has paid, then it may conclude that she has not suffered a loss as a result of taking the FSAVC. However, if a loss is identified Wesleyan should pay Ms C the value of the excess charges.

I’m aware that, despite several attempts, Wesleyan has been unable to obtain notional values from the in-house AVC scheme for other consumer’s in the same position as Ms C. This isn’t surprising given that the firm operating the scheme has changed over the years. So I have set out below details of the benchmark that Wesleyan should use to run the comparison.

Putting things right

As at the date of my final decision, Wesleyan should:

If it wishes to do so, calculate a notional value for the in-house AVC scheme as if it had performed in line with the FTSE UK Private Investors Income Total Return Index for half of the investment, and for the other half, the average rate from fixed rate bonds index.

I've chosen this benchmark because this would have achieved capital growth with a small risk to the capital. The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to their capital. The FTSE UK Private Investors Income total return index (prior to 1 March 2017, the FTSE WMA Stock Market Income total return index) is made up of a range of indices with different asset classes, mainly UK equities and government bonds. It’s a fair measure for someone who was prepared to take a small degree of risk to get a higher return. So, the 50/50 combination would reasonably put Ms C into that position. It does not mean that Ms C would have invested 50% of her money in a fixed rate bond and 50% in some kind of index tracker investment. Rather, I consider this a reasonable compromise that broadly reflects the sort of return Ms C could have obtained from investments suited to her objective and risk attitude.

Wesleyan should then compare the actual value of the FSAVC with this notional value. If the actual value exceeds the notional value no financial loss has been suffered and it need not take any further action.

The Financial Ombudsman Service uses benchmarks like this as a proxy for the typical growth that would have been achieved in investments that performed similarly to the benchmark. The aim of any benchmark used in this way is for the investment provider to achieve returns broadly in line with the benchmark, despite the charges that would ordinarily be incurred. For that reason, Wesleyan should not deduct charges when taking this particular step to calculate a notional value. This is consistent with the approach the Financial Ombudsman Service takes with such benchmarks.

If Wesleyan doesn't carry out the above comparison, or the comparison produces a loss, it must run a charges only calculation to establish the difference in charges between the FSAVC and in-house AVC. This should be run 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 a loss is identified Wesleyan should pay Ms C the value of the excess charges 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 add 8% simple per year on any loss from the date of my final decision to the date of settlement.

My final decision

For the reasons explained above, I uphold this complaint on the basis that Ms C would have joined her employer’s in-house money purchase AVC if she’d been suitably advised. I direct Wesleyan Financial Services Ltd to carry out calculations set out above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Ms C to accept or reject my decision before 6 July 2022.

Lorna Goulding
Ombudsman