DRN-3799280

The complaint

Ms B's representative has complained, on her behalf, that an appointed representative of Sesame Limited gave her unsuitable advice to establish a stakeholder pension plan instead of enhancing her occupation pension scheme (OPS) defined benefits by buying added years.

What happened

Ms B was advised by Sesame in November 2001 to establish a stakeholder plan with Standard Life and the policy was put in place in December 2001. Ms B's circumstances at the time were that she was 31, with no financial dependants. She was employed, earning just under £29,000 pa, was a member of the NHS pension scheme, owned her own (mortgaged) home and was considering buying and letting property.

An income/expenditure form demonstrated no significant income surplus, but she had savings of just under £9,000. Ms B wished to retire at 55 and she was making contributions to a Free Standing Additional Voluntary Contribution (FSAVC) policy with Scottish Equitable at £130 pm. But it was recorded that Ms B would be more comfortable making a lower contribution of £100 pm.

Ms B had a balanced attitude towards investment risk, and her objectives in terms of her retirement planning were to maintain her standard of living and plan for early retirement.

Sesame said that the advice given to Ms B by a previous financial adviser to establish the FSAVC policy had been right for her profession at the time, but recommended that she redirect her contributions to a stakeholder plan from then on. These would be invested 25% in the with profits fund, and 75% in the managed unit linked fund. There would be a maximum 1% pa charge, in line with stakeholder plan requirements.

Ms B's representative complained to Sesame in July 2021, saying that the recommended policy wasn't suitable for her needs, and that in particular Ms B had been unaware of the higher charges attached to it when compared to her "in house" options.

In response, Sesame said that Ms B's complaint had been raised too late under the rules contained within the regulator's handbook. It said that Ms B had been faced with an annual allowance tax charge in 2017 and she stopped her stakeholder pension contributions. It said that Ms B ought to have been aware of having cause for complaint about the original advice by this point, and she should then have complained within the three year period allowed for in the rules.

Dissatisfied with the response, Ms B's representative referred the matter to this service. One of our investigators, and consequently, following a rejection of that assessment by Sesame, an ombudsman, concluded that the complaint hadn't been raised too late and was therefore one which we could consider.

Our investigator then set out his findings on the merits of the case, saying the following in summary:

- The FSAVC review was a required course of action for policies taken out between April 1988 and August 1999, and so Ms B's policy hadn't fallen within its scope.

- But Regulatory Update 20 (RU20) issued by the Personal Investment Authority (PIA) in 1996 clarified the requirements for independent financial advisers (IFAs) on the sales of AVCs and FSAVCs.

- This required that IFAs discuss the availability of an added years arrangement within the OPS and the number of years which could be purchased. But despite the adviser's own recollections that this had been discussed, the available documentary evidence from the time of the sale didn't suggest that this had happened.

- The adviser had also said that Ms B's income was dropping as she was about to take an academic post and that Ms B required flexibility in regard to making contributions as she may take career breaks. The adviser further said that Ms B was thinking of switching to the University Superannuation Scheme and that she had some credit card debt which might have been a factor in reducing her contributions.

- Ms B was a late entrant to the NHS pension scheme and as she planned to retire at 55, she most likely would have had scope to buy added years. These were beneficial for people who remained with the same employer and envisaged salary increases.

- But it wasn't enough to say that, as Ms B was a doctor, with good job prospects and likely salary increases, added years would have been the suitable option.

- Ms B was, at the time of the advice, quite young to be committing to a career in the NHS. And added years represented poor value for individuals who left their OPS early or didn't have significant salary increases. They were also relatively expensive and inflexible.

- At the time of the advice, investment returns were projected to be higher than they are now, which might also have made added years a less attractive option.

- Ms B reduced her pension contribution from £130 to £100 pm, which meant that she'd already taken advantage of the flexibility offered by a "money purchase" arrangement – which wouldn't have been available through added years. It also demonstrated that Ms B had a preference for a lower level of contributions. Ms B was also single at the time, and so the additional dependants' benefits of added years would have been of little value.

- Ms B would have favoured the flexibility of being able to change her contribution level, and the charges for the stakeholder plan were capped at 1%, which would also have been appealing.

As such, the investigator concluded that Ms B was likely to have found the prospect of contributing to the stakeholder plan more appealing than buying added years.

Ms B's representative disagreed, however, saying the following in summary:

- Ms B had confirmed that she hadn't joined the NHS pension scheme late – she'd joined in 1994 – and nor had she said that she wished to retire early. But asking a client if they would like to retire early was a familiar method of mis-selling such policies.

- Ms B had reduced her contribution to the other FSAVC policy as she was taking on the additional stakeholder policy – not because she was flexing her ability to reduce her pension contributions. She had recently received compensation in respect of the earlier mis selling of her FSAVC policy.

- Ms B had never reduced her pension contributions and she only had a reduced income when she took an academic post on a temporary basis. This wasn't an unusual step for a doctor, and the University Superannuation Scheme was offered to all academics, but Ms B didn't seriously consider switching.

- Ms B had planned a lifelong career in the NHS and planned to remain in it until she was 70.

- At the time, Ms B was intending to marry at some point.

- There could be no doubt that the option of added years would have been the most suitable for Ms B. Flexibility of a stakeholder plan wouldn't have superseded the benefits of buying added years, and none of the other advantages of a stakeholder plan, such as a lack of job prospects, low salary increases or early retirement applied here.

- The IFA had been lacking in their responsibility to provide the necessary comparison between the stakeholder plan and in house arrangements.

As agreement couldn't be reached on the matter, it was referred to me for review.

I issued a provisional decision on 14 October 2022, in which I explained my reasons as to why I though the complaint should be upheld, but on the basis that Ms B should have been advised to start contributing to the in house AVC arrangement rather than buying added years. Those 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.

Having done so, I'm sympathetic to many of the points made by Ms B and her representative. As a doctor in her early thirties, and who had joined the NHS scheme around seven years earlier, I think it's more likely than not that she would have remained employed in the NHS and that her salary would have increased over the years, making her, on the face of it, a credible candidate for added years.

I've also noted what's been said about the level of contribution and the comments on what's been inferred from this relating to affordability concerns. Ms B has confirmed that she didn't reduce her money purchase contribution.

But Ms B's further confirmation that she hadn't joined the NHS pension scheme late, nor was she seeking to retire early, doesn't, I'm afraid, assist in persuading me that she would, or should, have opted to buy added years. If it was likely that Ms B would have, or be close to having, her full NHS pension entitlement, then there would have been little point in buying added years. Added years are only of value where an individual might not have 40 years' service within the "60ths" NHS scheme.

Ms B has in fact said that she intended working for the NHS until age 70, which would therefore mean that the money purchase option would have been the more advantageous for her, especially given her balanced risk outlook and, as the investigator has said, the likelihood of projected higher returns from such an arrangement at the time.

But I don't think the stakeholder plan, even with its 1% cap on charges, would have been of greater benefit that the likely even lower charging option of the in house AVC. And as with the investigator, I can't see that the available documentary evidence supports the position that Ms B's options in that regard were fairly brought to her attention or discussed.

IFAs had an obligation, which RU20 reinforced in 1996, to set out the differences between the in house arrangements and a free standing alternative. Although the recommendation was to establish a stakeholder plan, I don't think this changes the fundamental principle, which is that the in house AVC arrangement, due to the economies of scale in administration terms, was likely to be cheaper.

Therefore, on the basis of the likely difference in costs, I think the IFA ought to have recommended that she begin paying into the in house AVC arrangement. And had this been the case, I think Ms B would have accepted that recommendation.

Accordingly, I propose to uphold the complaint and I think compensation should be calculated on the basis of a comparison with the lower costs that would have been incurred if Ms B had begun paying into the AVC arrangement instead of the stakeholder plan.

<u>Putting things right</u>

Sesame Limited 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 (or as is the case here, the stakeholder plan) 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, Scottish Widows 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 B'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 B 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 20%. So making a notional deduction of 15% overall from the loss adequately reflects this."

Sesame said that it had no further comment to make, but Ms B said the following in summary:

- Her objection was that the information provided by the agent both purposefully and incorrectly portrayed her as someone who'd be unlikely to receive a full NHS pension due to her lifestyle.

- Examples of this misinformation were that she had been recorded as joining the pension late, had actively reduced her contributions and planned to take multiple career breaks and retire early at age 55.
- Ms B expressed surprise that they were upheld in this service's initial review.
- A career in medicine had always been her vocation. She qualified from medical school at 25 and after six years of training she immediately started full time work for the NHS.
- She'd been described in the provisional decision as a late entrant into the scheme, but this was the earliest that she could have entered the scheme as a doctor.
- She had a temporary pay cut whilst pursuing a PhD, but this was a sign of commitment to a long term career in the NHS rather of dwindling career prospects, as had been implied in the provisional decision.
- She didn't reduce her pension contributions during this time, and she had no intention of taking multiple career breaks, other than maternity leave in the future.
- Although she had been surprised when Sesame's representative had told her she could retire at age 55 and take her pension, it was never her intention to retire early.
- Other than the PhD, she had worked full time in medicine since 1994, taking only two maternity leave breaks.
- The provisional decision had commented that, at the time of the advice, she was quite young to be committing to a career in the NHS, but she found this comment strange in that the NHS was the only route of employment for those undertaking medical careers in the UK.
- It seemed perfectly reasonable that, at the age of 31, she recognised that the NHS would be her future employer until her retirement. She suspected that commentary around this wouldn't have been made if she was a male doctor of the same age.
- She was also unsure as to the relevance of her marital status in 2001 in terms of her eligibility for compensation.
- As a young doctor, she was often visited by financial advisers who attempted to frighten her with stories of how her pension would fail her in retirement. But luckily she was never persuaded to leave the NHS (as was the case with some colleagues).
- But she wasn't informed of the added years option. This was only brought to her attention in the summer of 2021 when she had a conversation with a friend.
- She had already stopped paying into her stakeholder plan in 2017 as a cost saving measure, but not because it had been mis-sold.

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.

I think there may be some confusion around my findings as set out in the provisional decision – either that, or Ms B has again referred back to the investigator's assessment in formulating her points as set out above.

To clarify, the comments which Ms B has attributed to me above were those of the investigator, which I summarised in the provisional decision, but which I in fact departed from in my own findings. I'd refer Ms B and her representative back to that provisional decision, but in summary, I said I was sympathetic to the points she had raised in response to the investigator's assessment. I said that I thought Ms B would have been more likely than not to have remained employed by the NHS and that her salary would have increased over the years. I accept that medicine is a vocational career in which employees are more likely than, say in other professions, to remain within until retirement.

As such, I said that, on the face of it, Ms B *was* a credible candidate for added years.

But there is then again, I think, confusion over why I don't think she would, or should, have been advised to buy added years – and this was precisely because of what Ms B had told us about her not being a late entrant to the scheme and that she didn't envisage retiring early.

This means that she would more likely than not have had her full entitlement to the defined benefit aspect of the NHS pension scheme, without needing to buy added years. A scheme member cannot receive more than 40/60ths (or 45/60ths in certain situations) of their final or average salary within the NHS scheme – this is the maximum defined benefit entitlement, and so it would have been pointless for Ms B to have bought added years if she was already predicted to be a scheme member for 45 years (having entered the scheme at 25 and retiring at 70) and so would have accrued 45/60ths within the scheme.

This is why Ms B would have been better off directing her contributions to the in house AVC scheme. And I hope that this clarifies the position and removes any prior confusion over what I had provisionally concluded and why, for those same reasons, it remains the case that I think Ms B would have been best advised to contribute to the in house AVC scheme.

Putting things right

Sesame Limited 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 (or as is the case here, the stakeholder plan) 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.

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If the calculation demonstrates a loss, the compensation amount should if possible be paid into Ms B'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 B 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 20%. So making a notional deduction of 15% overall from the loss adequately reflects this.

My final decision

My final decision is that I uphold the complaint direct Sesame Limited to undertake the above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Ms B to accept or reject my decision before 9 December 2022.

Philip Miller
Ombudsman