

## **complaint**

Mrs A has complained about the suitability of the advice given by The Prudential Assurance Company Limited ("Prudential") for her to contract-out of the State Earnings Related Pension Scheme ("SERPS").

## **background**

The adjudicator wrote to Mrs A in July 2013 with her assessment of the complaint. The adjudicator did not consider that the complaint should be upheld. This was because, in summary:

- Mrs A's earnings of approximately £8,000 per annum were well above the lower earnings limit at that time.
- Although Mrs A was over the pivotal age of 35 when she signed the Application, she signed a Disclaimer acknowledging and accepting that her pension could be lower by contracting-out of SERPS. Further, Mrs A backdated her decision to contract-out to 6 April 1987, so she would have been aged 35 at that time.
- At the time of the advice there was a reasonable prospect that contracting-out of SERPS could have been more beneficial.

Mrs A's representative did not agree with the adjudicator's assessment. He said that the advice to contract-out was not suitable because, in summary:

- There were a variety of factors that needed to be taken into account in assessing the suitability of the advice – Mrs A's attitude to risk, whether she understood the risks associated with contracting out of SERPS and her capacity to accept losses. These were more important than the arithmetical calculation of age, income and period to retirement.
- SERPS was effectively a defined benefit scheme and the key risk of opting out of it was that the benefits could ultimately be lower. The risk of lower benefits was not explained to Mrs A.
- There was no evidence that Mrs A's attitude to risk was properly considered in the advice given. It considered that the evidence now suggested that she wished to take little or no risk with the value of her pension fund.
- Mrs A could not have known what the risks of contracting out were, due to her lack of investment knowledge and her occupation, to be able to make an informed decision without advice from her financial adviser.
- Mrs A's attitude to risk was inconsistent with the risks that she would have needed to take in order to have her fund grow at a sufficient rate to give her a pension greater than remaining in SERPS.

Prudential made no further submissions.

## my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint. Having done so, I have come to the same conclusions as the adjudicator, and broadly for the same reasons.

As the adjudicator explained in her assessment, when the government decided to allow individuals to contract-out of SERPS, and offered incentives to encourage them to do so, it gave no advice as to who should be advised to remain in SERPS and those for whom it was expected that contracting out would be beneficial. So pension providers' actuaries carried out comparisons of the projected benefits from SERPS with those from an alternative personal pension arrangement. These calculations were based on what were felt to be conservative assumptions of likely future investment returns at the time. The rebates paid by the Government were set in such a way that it was more attractive for younger individuals to contract-out than those who were older - the ages, where the provider's advice as to whether to contract out or not changed, were called pivotal ages.

Prudential's actuaries determined that the pivotal age for women was 35. This meant that it was anticipated, on the *conservative* assumptions used, that women aged below 35 would be better off contracting-out rather than remaining in SERPS. Mrs A was just over age 35 at the time, and although the contracting out was backdated to two year earlier the period of investment would be lower than assumed for someone aged 35. However Mrs A signed a disclaimer confirming that she understood and accepted that her policy could provide a lower pension by contracting-out of SERPS.

As well as age, another of the factors that were used to determine whether someone was likely to be better off contracting out of SERPS was their earnings. Mrs A's annual earnings were recorded at the time of the advice as being approximately £8,000, and this was considered to be sufficient to ensure that the rebates forwarded by the Department of Social Security ("DSS") would cover the applicable charges.

So, at the time, although there was the potential for Mrs A to be better off at retirement by contracting out of SERPS it was not guaranteed. It depended on the actual returns provided by the fund that the rebates were invested into and the rates at which the fund was turned into pension at retirement date (called annuity rates).

Accordingly, as noted by Mrs A's representative, there was a risk that the benefits payable from the pension with Prudential could be lower than what would otherwise have provided by SERPS. The representative has said that the policy was unsuitable because Mrs A was not willing, and did not have the capacity, to accept the risks of opting out, and the risks were not explained to her.

Whilst I understand the points that the representative has made about the factors to consider in assessing suitability, I think the key point is that there was a risk that the benefits may not be as high as provided by SERPS. Mrs A specifically signed to say at the time of contracting out that she understood that "...my total pension could be lower by contracting out of SERPS." I am satisfied that this is a clear statement and readily understandable to a layperson. And in 1994 Mrs A signed to say that the advantages of contracting back into SERPS had been explained and she understood that re-joining SERPS may give her higher benefits than remaining in the Prudential pension. However she chose not to contract back in. So I think it is reasonable to conclude, on balance, that Mrs A was likely to have been aware that there was a risk in contracting-out and that it follows she was willing to accept that risk.

Mrs A contracted-out in 1989 and these matters should be considered in the light of what was considered reasonable at the time. Unfortunately the investment returns achieved by the underlying fund have been much lower than would have been reasonably expected, and this combined with the lower annuity rates now available to convert funds into pension has meant that the expected gains from contracting out have not arisen.

However, it seems to me that contracting out provided a reasonable prospect of Mrs A improving on the benefits that she would otherwise have received from SERPS – albeit it involved some risk. But in my view this would not have appeared to present a significant risk at the time, and the evidence suggests that Mrs A had been alerted to and was willing to accept some risk.

Accordingly, having carefully considered the matter, I have not been persuaded that contracting-out of SERPS was inappropriate for Mrs A given her circumstances at the time.

**my final decision**

My final decision is that I do not uphold Mrs A's complaint.

David Ashley  
**ombudsman**