DRN-4207604

The complaint

Ms B's representative has complained, on her behalf, about the advice she received in 1994 and 1999 from Colonial Mutual (now Aviva Life & Pensions UK Limited) to establish and then top up a Free Standing Additional Voluntary Contribution (FSAVC) pension policy.

What happened

Upon the advice she received in 1994 from a representative of Colonial Mutual, Ms B established the FSAVC policy. She was at the time at teacher, had been a member of the Teachers' Pension Scheme (TPS) since 1989, and was keen to increase her pension provision. She began paying a monthly contribution of £53.

Ms B then topped up her contributions in 1999 by a further £26 pm.

Ms B's representative complained to Aviva on her behalf in March 2022, saying that she should have been advised to capitalise on the "in house" AVC alternative associated with her membership of her employer's defined benefit occupation pension scheme.

Aviva accepted that it couldn't confirm whether Ms B had been informed of the "in house" AVC alternative in 1994, and as such it upheld her complaint and agreed to undertake a "charges only" loss assessment.

But it said that it would cap its liability at the point of Ms B topping up her contributions in March 1999. At this point, Aviva said, Ms B signed a document which stated that she had obtained information from her employer regarding her "in house" options, was aware that charges on an FSAVC policy were likely to be higher than those on the "in house" option – and that she was happy to proceed on that basis.

Aviva said that Ms B was therefore aware of her options and that she made an informed choice on that basis. As such, it reiterated that it would only be undertaking the loss calculation on the initial premium rather than the top up amount.

Dissatisfied with the response, Ms B's representative referred the matter to this service. One of our investigators assessed the complaint and thought it should be upheld, saying the following in summary:

- He was satisfied that, when arranging the top up premium in 1999, the leaflet drew Ms B's attention to the "in house" alternative and directed her to her employer for further information on this.
- But the rules in place in 1999 also required the representative to discuss with Ms B the generic differences between the FSAVC policy and the "in house" alternative.
- Aviva hadn't demonstrated that such a discussion occurred, and so the investigator said that he couldn't know what was discussed with Ms B. The declaration within the leaflet also didn't set out what had been discussed, he said.

- As such, the investigator said that he hadn't seen enough to persuade him that the advice in 1999 was complaint or warranted Aviva capping its liability at that point.

Ms B's representative accepted the investigator's conclusions, but Aviva didn't, saying the following:

- It wished to point out that it hadn't conceded that the FSAVC policy was unsuitable for Ms B, but rather it hadn't been able to evidence that Ms B was told about the alternative options in 1994.

- The literature provided to Ms B in 1999, and signed by her, confirmed her understanding of the top up policy. It was clear that the available options were pointed out to Ms B and that the charges in the "in house" AVC could be lower.

- As a "tied" adviser, the representative wasn't able to contact the scheme administrators to obtain further details, and at the time this wouldn't have been expected of them.

- The representative had met the requirements under "RU20", the codification of procedures which the regulator said businesses should implement when providing advice on FSAVC policies.

- It acknowledged that it hadn't been able to find a "reasons why" letter, but it was unlikely that this would have contained anything other than what it had confirmed in the literature which was provided to Ms B and signed for.

- The investigator therefore seemed to be expecting a different level of selling practices than those which were required at the time.

The investigator replied, saying that the provision of the leaflet wasn't enough to demonstrate that a discussion had taken place, as was required by RU20.

Aviva continued to disagree, however, querying as to why Ms B would have signed to say that she understood the content of the leaflet if it hadn't been discussed. And Ms B's signature on the document was a testament to her full awareness of the alternatives.

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

In response to confirmation of this, Ms B's representative asked that the ombudsman review the "complete complaint", which included Ms B not being made aware of both in house options – the money purchase AVC arrangement and the added years alternative.

I issued a provisional decision on the matter on 18 May 2023, in which I set out my reasons as to why I thought the complaint should be upheld. The following is an extract from that decision.

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

I've noted what both the investigator and Aviva have said about the leaflet, Ms B's signature on it and Aviva's view that this would have meant that a discussion had been held and that Ms B was therefore aware of the alternatives.

I accept that Ms B was likely aware of the alternatives as a result of the leaflet which she signed to attest to having received it. Although, as with the investigator, I don't think this necessarily evidences that a discussion was held about the alternatives or the differences between them. For example, I can see no wording within the leaflet along the lines of "as discussed…" or "as set out in the suitability report…".

But there is in my view a more significant issue here, specifically with regard to the "in house" AVC option (see further below about "added years") and one which goes to the heart of the rationale as to why such cases might be upheld. And that's Ms B's awareness of the likelihood that the charges under the "in house" AVC arrangement would be lower.

To clarify, the Personal Investment Authority (the regulator at the time) said that, before selling an FSAVC policy, tied advisers should:

- *Draw the consumer's attention to the "in house" alternative*
- *Discuss the generic differences between the two routes '(taking account, among other things, of the features described in this article)'*
- *Direct the consumer to his employer or the OPS for more information on the in-house option*

RU20 mentioned the tax treatment of contributions and benefits, employers being willing to match or top-up benefits, and the ability to provide additional life cover within its general introduction.

It also referred to the lower charges under an "in house" AVC arrangement in general terms, saying the followings:

"Charges under in-scheme AVCs will usually be lower than those under FSAVCs, reflecting economies of scale, rebated commission or a contribution to administration expenses by the employer. Of all the differences between the two routes, this is likely to exert the greatest impact on which route would offer the greater benefits to the client."

It therefore expected it to be known by (even tied) advisers that the charges under the "in house" AVC arrangement were likely to be cheaper than the FSAVC policy alternative.

But the leaflet provided to Ms B didn't say this. It said that the charges in an "in house" arrangement can be lower. And I think that's an important difference. I think it's more likely than not that setting out the likelihood of charges being lower in the in house arrangement would have given Ms B pause for thought on what would quite reasonably have been the most significant deciding factor about how to proceed – the costs of the arrangements and the effect this would have on the final value of her plan.

And so, irrespective of whether there was a discussion about the points covered within the leaflet (albeit for the reasons given above, I agree with the investigator that there's no actual indication that one took place), I don't think it's been adequately demonstrated that Ms B was aware of this important fact.

And on that basis, my view is that the complaint should be upheld, and that the loss assessment on the "charges only" basis should include the top up premiums paid from 1999 as well.

I've noted the comments from Ms B's representative, asking that I consider all aspects of the complaint, including the "added years" alternative. I should point out that this aspect wasn't included within the complaint form submitted to this service. Rather, the matter which the representative wished us to consider was that of the Aviva proposing to cap its liability on the "charges only" loss assessment in 1999.

But at my request, the investigator has further enquired as to why Ms B's representative considers that added years might have been the appropriate alternative. In response, it's said that Ms B joined the TPS in 1989, when she was 25. When she met with the financial adviser, her annual salary was £16,410, she was single, she was intending to remain in the teaching profession (as she has) and her career prospects were good. She was keen to maximise her pension provision as much as possible, and due to her age when she started teaching and small breaks in service, she wouldn't have achieved her maximum number of years' service.

It further said that, at the time, Ms B was young and inexperienced, and not in a position to take risks with her pension provision.

And so I've thought carefully about the prospect of Ms B, had she been made sufficiently aware of her rights under her occupational pension scheme options (as was required of tied advisers in both 1994 and 1999), choosing to buy added years instead of money purchase AVCs.

The cost to Ms B at the time would have been around 0.7% of salary for each added year (for the 30 years left to age 60), and Ms B was paying around 3.9% into her FSAVC policy from 1994, and then a total of approximately 4.3% from 1999 after the "top up". As Ms B had accrued five years' service by 1994 and was 30 years old. She could have maximised her defined benefit pension entitlement at a normal retirement age of 60 through buying five added years, which would have amounted to a lower overall contribution than she was making to her FSAVC policy.

There are several considerations when thinking about Ms B's options in 1994. She was relatively young, but I think after five years' teaching, she would have been reasonably confident as to her tenure in the teaching profession and her possible career prospects.

As Ms B was single, she (or rather any dependants) also wouldn't have benefitted from the spouse's/dependants' benefits which would be produced in the event of her death through buying added years. The FSAVC policy, on the other hand, would have paid out the policy value upon her death.

Buying added years would also have been a significant commitment, as this needed to be sustained for the rest of her teaching career.

I think such downsides would have been of diminished importance to Ms B at age 30. She was clearly serious about, and committed towards, enhancing her pension provision, and was in a position to do so both in 1994 and 1999.

But I don't agree with Ms B's representative that she couldn't afford to take risks with her pension provision. She was single, with no dependants and was clearly in a position to make quite healthy further contributions to her pension. She had the "backup" of the defined benefit occupational pension scheme membership, was prepared to invest in a "managed" fund (which, given the likely number of years of investment I don't think would have been unsuitable or incongruous) and at the time, the returns on money purchase contributions would have seemed attractive, with the mid-band yearly growth projection being 9%.

But moreover, I do also need to take account of the content of the leaflet provided to Ms B in 1999 and the quality of the information this conveyed to her. And whilst, for the reasons given above, I think that the information was lacking in terms of Ms B's likely consequent awareness of the advantages of the "in house" AVC route (with particular regard to charges), I think that the leaflet fairly set out the aims and features of buying added years. And I think Ms B would have been in a sufficiently informed position to then make further enquiries about this option if it interested her – which is what was required of tied advisers, as they couldn't actively advise on an "in house" route.

Ms B proceeded to top up her contributions to the FSAVC policy in 1999 rather than investigate the added years option. And I therefore think that it might reasonably be inferred that Ms B would have made the same decision in 1994, had she been provided with the same information.

Overall, therefore, I'm satisfied that Ms B more likely than not wouldn't have opted to buy added years in 1994, as she similarly didn't in 1999, but I'm currently of the view that the complaint should be upheld on the basis that Ms B, properly informed, would more likely than not have opted to contribute to the "in house" AVC arrangement in both 1994 and 1999.

<u>*Putting things right*</u>

My aim is to put Ms B, as closely as possible, into the position she would now be in had she been fully informed about the AVC option in 1994 and 1999.

Aviva should therefore undertake a redress calculation in accordance with the regulator's FSAVC review guidance for both the original contributions from 1994 and those then made from 1999, 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, Aviva 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."

Aviva hasn't responded to the provisional decision. But Ms B's representative has said the following in summary:

- The cost for Ms B to buy additional years' service was unknown without an actuarial calculation, but it agreed that she could have bought a significant number of years with the contribution she was making to her FSAVC policy. Added years were therefore affordable for Ms B.

- It had always been its opinion that most public sector workers would have chosen the guaranteed option of added years rather than the risk based product.

- It agreed that Ms B was likely to remain in the teaching profession and therefore also likely to have good career prospects and salary increases.

- It wasn't unusual for a female aged 30 to be unmarried with no children, but if she had been married with children, it would be arguable that this would have meant time out from her career, leaving a larger pension shortfall which would be unaffordable to make up.

- When she established the FSAVC policy, Ms B's priority was to maximise her pension provision in the safest way, and it seemed very harsh to take the view that, just because she had either chosen to remain single or hadn't met the right partner, she wouldn't have bought added years. As she had 30 years left to retirement, it was probable that she would have met someone.

- The argument that, as she was single, the death benefits from the FSAVC policy would be more beneficial seemed contradictory to the fact that she had no financial dependants. This wouldn't therefore justify Ms B opting for the FSAVC policy over buying added years.

- Although added years would have been a career-long commitment, Ms B was prepared to do this, as has been evidenced by her contribution record since.

- When it had said that Ms B couldn't afford to take risks with her pension, this wasn't meant in monetary terms, but more in terms of "provision". Ms B wished to build up as much pension provision as possible. She was young, single, and had no experience of pension or investment matters.

- If Ms B had been willing to take a risk, it would surely have been reasonable to expect her to invest in something other than a managed fund, for example 100% in an equity fund. It also wouldn't be unreasonable to expect to see fund switches throughout the term of the policy, but there had been none.

- It had already been agreed that Ms B was able to achieve maximum years' service in the guaranteed added years environment, but having the main scheme as a backup wouldn't justify the taking of risks with the FSAVC policy. Every public sector worker had that "back up" and this rationale would imply that no or very few public sector workers would ever have bought added years.

- The growth expectations, whilst likely appealing at the time, had been reduced by the regulator since. The projections therefore didn't carry much weight in the argument, especially when there was no evidence that Ms B had been advised to contact the main scheme for an added years quote so that she could make the comparison between the two arrangements.

- The information contained in the brochure may have set out the different options available, but this wasn't enough to fairly say that the adviser had complied with the regulatory requirements. The guidance required a discussion, and it appeared that I'd agreed with this by removing the cap on liability proposed by Aviva.

- As there was no evidence of a discussion, it seemed extremely unfair to deem the brief mention of added years in the brochure as being sufficient to say that Ms B wouldn't have bought added years.

- There was no dispute that the advice given to Ms B in 1994 was wrong – and it was very unlikely that, had the correct advice been given, she would have changed her view later on. It was also debateable as to whether the further appointment for the top up in 1999 would have taken place had suitable advice been given in 1994, as Ms B wouldn't have needed to seek further advice. It therefore brought into question the importance of the brochure in this case – and the representative thought that this was none, given my finding that the sale in 1999 was non-compliant.

- As I had deemed the sale of the top up in 1999 to be non-compliant due to the lack of evidence surrounding a discussion, it therefore followed that there was no evidence of a discussion around added years. It seemed unfair to have one rule for the money purchase arrangement and one for the added years arrangement. The regulator didn't differentiate between the two.

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've noted the points made by Ms B's representative, and would comment as follows.

Firstly with regard to its opinion that most public sector workers would have chosen the guaranteed added years option rather than the risk based FSAVC policy or in house AVC option, this service considers individual complaints - and so the individual circumstances which were relevant at the time of the disputed advice, rather than opinion-based assumptions about a wider group of individuals. And it is Ms B's particular circumstances and objectives which have been considered here.

Addressing the point about the hypothetical situation of Ms B being married with children and the larger gap which this would leave if she'd taken time out from her career to raise children, I think Ms B would more likely than not have identified the shortfall in her pension provision and simply made it up in what she considered to be the best possible way. Simply because Ms B may have had more years missing wouldn't make it more or less likely, in my view, that she would have chosen to buy added years. And I can't see why it reasonably would. An individual doesn't need to make up all of the missing service – they can chose to buy as many added years as they wish up to the scheme maximum.

As to the assertion that I've judged Ms B harshly by referring to her single status as a reason for her choosing a money purchase arrangement over buying added years, this simply refers to her capacity, at the time, to take financial risks and her likely diminished concern about the lack of spouse's benefits which would be produced by the added years.

And I think Ms B's representative may have misunderstood the point I was making about the death benefits which would be produced by the FSAVC policy. These would be paid as a lump sum to nominated beneficiaries (at the discretion of the trustees) from a money purchase arrangement, for example to other family members. Whereas the death benefits from the main scheme would be payable only to a spouse or financially dependent children. And so her single status at that time is of some relevance.

I do agree that Ms B would likely have been committed to her pension saving, as may have been demonstrated since. And I also agree that Ms B would likely have wished to build up as much as possible. But I don't think that this either would have been, or Ms B would have viewed it as being, incompatible with a fairly mainstream pension product such as an AVC arrangement, especially given the growth projections in place at the time.

And I'm not sure I follow the rationale relating to the representative's view that, if Ms B had been willing to take a risk with a part of her pension provision, she would have invested in something like a 100% equity fund. I think a managed fund, with the associated diversification of assets, would have offered a sufficiently risk/reward based environment. And for individuals lacking investment experience, as has been asserted as being the case for Ms B, this type of "default" fund can be the most appealing. I don't think a willingness to take some financial risk translates directly across to an individual being highly speculative, as seems to be the suggestion here.

Ms B's representative has further said that the "backup" of the main scheme guaranteed benefits wouldn't justify Ms B taking a risk with her additional provision. But Ms B may well have thought so, and again, although I note the generalisation about this type of rationale meaning that no or very few public sector workers would ever buy added years, I've considered Ms B's individual circumstances and whether I think she in particular is more likely than not to have opted for added years. For other individuals, the situation will be different.

I've then noted the commentary about the growth projection rates at the time, and that these were reduced over subsequent years. But I'm considering the position and information available at the time, not over subsequent years and whether by a later point such growth projections might have been deemed to have been optimistic. And whilst I don't think that Ms B necessarily needed to know what she could have achieved in terms of the monetary amount from buying added years to be able to appreciate the monetary value of what she could receive from an AVC policy, I in any case remain of the view that she would reasonably have been aware of the added years route/option from the information contained in the leaflet.

I note that Ms B's representative takes a different view, and that it has said that I had agreed that a discussion was required, as set out in the regulatory requirements, and that it was the basis of my provisional decision that this hadn't happened – and so the cap on liability should be removed.

But this wasn't the basis of my provisional findings. I in fact said that it couldn't be demonstrated either way as to whether a discussion had been held. But conscious of the requirement that information relating to Ms B's options be fairly brought to her attention, I considered the content of the leaflet to determine, on a fair and reasonable basis, whether Ms B would more likely than not have been aware of the option of buying added years.

And my conclusion, on the basis of the leaflet which she signed to attest to having read it, was that Ms B was more likely than not to have been aware of the option of added years. And my rationale for clearly distinguishing between the information provided about the added years option and that for joining the in house AVC scheme was that the detail relating to the latter didn't meet the bar of what was expected – in that I didn't think Aviva had been clear enough in setting out that the AVC charges were likely to be lower than for the FSAVC policy.

I did, however, conclude that the information relating to the added years option was clear enough. And I agree that Ms B would have demonstrated a consistency of behaviour between 1994 and 1999. And so, given that I think she would reasonably have been sufficiently aware of the option of added years in 1999, and nevertheless chose the money purchase option, I think it's more likely than not that she would have made the same decision in 1994 if she'd been presented with the same information.

I've further noted the representative's comment about the leaflet being of no importance given that, had suitable advice been given in 1994, Ms B wouldn't have needed to meet with the adviser again in 1999. But we base our decisions on the facts of the case. And the fact is that, in 1999, Ms B was provided with the leaflet which set out the option to investigate buying added years, but instead chose the money purchase route.

Overall, therefore, my view remains that Ms B wasn't in a well enough informed position in 1999 to decide whether to choose between the in house AVC scheme and the FSAVC policy, and so the liability shouldn't be capped for that redress calculation in 1999. But I do maintain that Ms B was sufficiently well informed to be able to decide whether to investigate the added years option. And as she didn't in 1999, I think it's more likely than not that she would have made the same decision, with the same information, in 1994.

Putting things right

My aim is to put Ms B, as closely as possible, into the position she would now be in had she been fully informed about the AVC option in 1994 and 1999.

Aviva should therefore undertake a redress calculation in accordance with the regulator's FSAVC review guidance for both the original contributions from 1994 and those then made from 1999, 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, Aviva 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.

My final decision

My final decision is that I uphold the complaint and direct Aviva Life & Pensions UK 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 31 July 2023.

Philip Miller
Ombudsman