DRN-4535150

The complaint

Mr S's representative complains that Berkeley Morgan Limited (BML) incorrectly advised him to take out a Free Standing Additional Voluntary Contribution (FSAVC) plan, rather than join his employer's cheaper, in-house Additional Voluntary Contribution (AVC) scheme.

Mr S would now like BML to see if he's lost out financially because of their advice and recompense him accordingly.

What happened

In October 1996, Mr S, who was about to turn 23 years old at the time, met with an adviser from BML for advice on his retirement planning needs. He was already a member of his firm's final salary pension scheme and wanted to explore options for increasing his benefits at retirement. After reviewing Mr S's circumstances, BML recommended that he set up a FSAVC plan with a monthly premium of £30 and a term until his 55th birthday. On 31 December 2016, Mr S was made redundant after working for the same firm for over 20 years.

In October 2021, Mr S saw an advert from a claims management company (CMC) highlighting that consumers who took out FSAVC plans in the 1990s may have been misadvised. So, he contacted the CMC who, after discussing Mr S's circumstances with him, then submitted a complaint to BML on his behalf in March 2022. In summary, Mr S's representative told BML that their original advice to take out a FSAVC was inappropriate as they'd not properly considered the in-house AVC scheme, which they say BML should have recommended as it was a more cost-effective option than the FSAVC.

After reviewing Mr S's concerns, BML couldn't initially find any evidence that they had advised Mr S. However, after later being provided with an application form, they conceded it was likely that they had been involved in the advice. After considering the complaint, BML said that they felt it had been made outside of the regulator's time-limits that consumers have to raise their concerns with the provider and as such, they weren't going to consider the merits of his complaint. They went on to explain that as Mr S had received regular annual statements, he should have known earlier that there might be a problem with the original advice and as such, he should have contacted them sooner to raise his concerns.

Mr S was unhappy with BML's response, so he referred his complaint to this service. In summary, he repeated the same concerns, namely that BML should have recommended the cheaper in-house AVC scheme to him, rather than advise him to take out the more expensive FSAVC.

As BML didn't think that Mr S's complaint was one that this service could consider, an Investigator issued an initial view saying that, despite Mr S having received regular statements, that wouldn't have prompted him to think that there might be something wrong with the advice that he received in 1996. Our Investigator concluded by stating that they considered Mr S's concerns had been raised within the regulator's time limits – namely that he had complained within three years of when he became aware (in 2021) that there may be a problem with the original advice that he had received. As BML didn't agree with the Investigator's view, they asked for an Ombudsman to decide whether this service could consider Mr S's concerns. BML also explained that as they hadn't received any commission on the plan for over ten years, at some point between 1996 and 2012, Mr S must have taken advice from another adviser, to whom the commission payments would have been switched. BML felt that the introduction of another adviser should have involved the consideration of the FSAVC policy and any complaint should reasonably have been identified.

After considering the facts of the case, an Ombudsman said that he wasn't persuaded that having received the annual statements would've prompted Mr S to believe that anything was wrong with BML's advice sooner. That's because, he said, he'd seen no evidence of Mr S being provided with a comparison of costs on the in-house AVC compared to the FSAVC that BML arranged, so he wouldn't have known that he had cause for complaint. The Ombudsman also felt, in summary, that even if Mr S had taken advice from a new IFA, it was more likely than not that they hadn't made him aware of a potential problem with the original FSAVC advice and so any failing on the part of any subsequent adviser, who may have looked at Mr S's FSAVC policy, still wouldn't confer on Mr S himself an awareness of cause for complaint. The Ombudsman therefore concluded that this service was able to look into Mr S's concerns.

The complaint was then passed back to one of our Investigators who, after considering Mr S's concerns, issued a view saying, in summary, that having looked at his circumstances at the time, a proper comparison of the in-house AVC versus the FSAVC wasn't undertaken. She also didn't think that having looked at Mr S's circumstances, BML had demonstrated the FSAVC was in his best interests.

BML, however, disagreed with our Investigator's findings. In summary, they said that they felt that the FSAVC was suitable for Mr S because:

- He needed a plan that was flexible as, given the line of work that he was in at the time (working in retail store), Mr S didn't intend on staying with his employer long term. BML said that they felt their suitability letter to him clearly set out his plans to move employers in the future.

- The in-house AVC scheme was run by Equitable Life who three years after Mr S took the plan out, had to be rescued. BML also said that they wanted details of the AVC scheme so that they could compare what had actually happened.

- The adviser had clearly explained the differences between the FSAVC and the AVC and directed Mr S to his employer to obtain a benefit projection statement.

- They went on to say that Mr S was referred back to his company for details of the AVC and, they say, they provided full details to him of both FSAVC and in-house options.

Our Investigator was not persuaded to change her view as she didn't believe BML had presented any new arguments she'd not already considered or responded to. BML then asked the Investigator to pass the case to an Ombudsman to review that outcome.

After carefully considering the complaint, I decided to issue a provisional decision on the case as, whilst I was minded to uphold Mr S's complaint, I wanted to add wider context to that provided by our Investigator.

<u>What I said in my provisional decision:</u>

The purpose of my decision isn't to address every single point raised. My role is to consider the evidence presented by Mr S and BML, in order to reach what I think is an independent, fair and reasonable decision based on the facts of the case. In deciding what's fair and reasonable, I must consider the relevant law, regulation and best industry practice, but it is for me to decide, based on the available information that I've been given, what's more likely than not to have happened. And, having done so, I'm upholding Mr S's complaint and it's broadly for the same reasons as our Investigator. I'll explain why below.

Given that BML advised Mr S to take out the FSAVC over 20 years ago, I've looked at what rules were in place by the various regulators at that time. As BML was an independent adviser, they were required to follow the Financial Intermediaries, Managers and Brokers Association (FIMBRA) rules. The Personal Investment Authority (PIA), a predecessor of the Financial Conduct Authority, adopted the FIMBRA rules when it took over from FIMBRA in 1994. But, in 1988, FIMBRA said that an adviser should:

- *Not make a recommendation unless it believed, having carried out reasonable care in forming its belief, that no transaction in any other such investment (of which it ought reasonably to be aware) would be likely to secure the objectives of the consumer more advantageously.*

- *Take reasonable care to include in any recommendation to a person, other than a professional investor, sufficient information to provide that person with an adequate and reasonable basis for deciding whether to accept the recommendation.*

That meant BML was required to find out how all of these issues applied to the FSAVC and the various in-house options and anything else that might have been relevant to Mr S's situation, such as the sorts of funds within the AVC which may have been available for investment. They would then have needed to explicitly compare what the in-house options and what the FSAVC had to offer. So, this meant that BML would have needed to have gone further than a tied adviser, by looking into all the in-house options and positively recommending the suitable option and they would have to actively make a recommendation in the best interests of the consumer.

In May 1996, five months before BML's advice to Mr S in October 1996, the PIA issued Regulatory Update 20 (which is sometimes referred to as RU20), codifying the procedures it expected advisers to follow. The PIA was simply restating what FIMBRA already expected, saying that before selling a FSAVC, IFA's should include:

- *The difference in charges and expenses between the FSAVC and AVC.*

- *The choice of investments.*

- *The availability of added years and the number of years that could be purchased.*

- *The degree of personal control and privacy.*

- *The age at which benefits could be taken.*

- *The degree of portability on changing jobs or becoming self-employed.*

Even in the more general introduction to the article, RU20, it mentions the tax treatment of contributions and benefits, employers being willing to match or top-up benefits, and the ability to provide additional life cover. The article also refers to the lower charges under an in-house AVC in general terms. It says: '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.'*

As BML are an independent financial adviser, they were required to go a step further than tied advisers (who only advise on the products of one provider) at the time. The regulations not only required them to highlight the availability of in-house AVCs but IFAs were also required to undertake a comparison between the two. And having carefully considered BML's suitability letter to Mr S at the time, I don't believe that they went far enough in their obligation to provide Mr S with the balanced comparison that the PIA required of them at the time. I'll explain why:

BML sent Mr S a suitability letter on 28 October 1996, setting out their reasoning why a FSAVC was more appropriate for his circumstances than an in-house AVC. BML were required to have investigated and then set out the difference in the charges between the FSAVC and in-house AVC over the term of the plan, but their letter of 28 October 1996 was silent on costs. Whilst I've not seen the costs of Mr S's in-house AVC, typically (but not always), it would be cheaper. That means, BML should have simply recommended the money purchase in-house AVC, if this was the only in-house option and it had lower charges than the Legal and General FSAVC that they recommended. And that's because, as I've already explained, the PIA said in RU20, of all the differences between the two routes, lower charges were likely to have the greatest impact on the consumer's decision.

As BML didn't explore costs in their suitability letter, we don't know what difference there was in charges between the two plans, but working on the basis that the in-house scheme was cheaper (as they usually are), and taking account of Mr S's specific circumstances at the time – I think it's more likely than not that had BML highlighted the lower costs of the in-house AVC scheme, he would've selected that option. I say that because he was relatively young at the time of the advice, appeared to have very modest financial means (with a net disposable income of £200 per month), saving only £30 per month towards his goal and he didn't appear to have a need for what was likely to have been a more expensive arrangement that would require ongoing regular advice.

Whilst BML did undertake a limited comparison of the benefits between an AVC and a FSAVC, it wasn't tailored to Mr S's individual circumstances. Their letter explained that should Mr S move employers or become self-employed in the future, the FSAVC could be taken with him to his new role or converted into a personal pension. However, it seems to me that BML didn't actually explore the likelihood of Mr S moving jobs to understand whether that feature would be useful to him because, as it transpires, he stayed with the same employer until being made redundant some 20 years later in 2016. The letter also explained that as the in-house AVC option only offered a with-profits fund, the option to utilise either a discretionary or managed fund would better match his medium attitude to risk. But, I think in light of Mr S's modest premium, a discretionary managed fund (which is typically more expensive) would have been of little benefit to him and likely cost him more each month in charges.

In addition, BML wrote the FSAVC's retirement age to 55 when the scheme's normal retirement age was 60. I think that BML's letter was misleading because prior to 1999, Mr S would have had to take the FSAVC at the same time as his normal scheme benefits, so this perceived benefit wasn't actually beneficial to him. In any event, given Mr S was only just turning 23 at the time of the advice, I well suspect that he would have preferred to maximise his retirement income over the perceived additional flexibility that the FSAVC may have provided him.

I've also thought about the timing of BML's suitability letter to Mr S – which was issued to him on 28 October 1996, the same day that he signed the FSAVC application form. Whilst BML suggested that Mr S might want to contact his employer to obtain benefit projections, that appeared to relate purely to what his main scheme would likely provide at normal retirement age rather than the costs of the in-house AVC scheme. In addition, in response to our Investigator's view, BML explained that Mr S was referred back to his company for details of the AVC. But, I've not seen any evidence to confirm that he was – BML's letter only suggested that he speak to his employer to obtain details of the benefits from his main scheme, rather than the in-house AVC option. So, even had the potential for lower charges been brought to Mr S's attention at the meeting on 28 October 1996, he wouldn't have been in a position to explore that further because BML proceeded with the FSAVC application form the same day.

I've also thought about what BML have said about Equitable Life, the provider of the in-house AVC scheme. BML explained that it was well known in 1996 that Equitable Life were struggling financially and as such, Mr S decided against investing in the in-house AVC option because of concerns relating to the financial strength of that provider. As I wasn't present at the meeting in 1996 so I don't know what was discussed, the suitability letter is silent on that discussion and from what I've read, it appears the extent of Equitable Life's financial situation wasn't well known until the later stages of the 1990s.

In their recent submissions to this service, BML have again questioned whether this service has the jurisdiction to hear Mr S's complaint. Whilst I should explain that the earlier Ombudsman's decision stating that this case is a complaint we can hear is final, I did want to address a further point that BML have raised. BML initially said that as they haven't received any commission from Mr S's plan for over ten years, that suggests that another adviser provided him with advice on the plan at some point between 1996 and 2012. BML believe that adviser should've then identified that Mr S had cause for complaint and put him on a path of discovery sooner that there might be a problem with the original FSAVC advice.

However, BML later explained that they believed when Mr S's adviser from 1996 left their employment, he contacted Mr S, attempting to encourage him to move his plan to him under that new agency. Mr S has explained that after taking advice from BML, he didn't then subsequently seek direction from a new adviser in the years that then followed. He went onto explain that he recalls BML contacting him following the advice to explain that his adviser had left, but he didn't then meet with anyone else. I've not seen any evidence that Mr S was provided with any further advice on the plan but in any event, had Mr S spoken to his old BML adviser once he'd started work at his new firm, given that same IFA originally recommended the FSAVC and still, according to his recent statement to this service stands by his original advice, I don't believe that Mr S would've known sooner than he did that there was a problem.

Summary

BML's letter wasn't particularly balanced, it only noted disadvantages of the in-house AVC scheme and didn't highlight any drawbacks with the FSAVC route, such as the difference in costs. So, it seems to me that Mr S wasn't placed in a fully informed position and had BML followed the regulator's RU20 briefing which was issued in May 1996, five months prior to their advice to Mr S, they should have been aware of the PIA's requirements to specifically set out the in-house AVC costs to Mr S at the time. As BML have failed to follow the regulator's rules at the time of their advice to Mr S, and I'm not persuaded that he needed a FSAVC over an in-house AVC option, I am therefore upholding his complaint and require BML to take the following actions to establish whether Mr S has suffered a loss.

Responses to my provisional decision

After receiving my provisional decision, Mr S didn't provide any further comments.

However, BML stated that they didn't agree with the provisional decision, and in summary, they said:

- They had sought permission from the complainant to consider the issue of costs more closely. BML went on to say that, as the in-house AVC was provided by a third-party firm who at the time were under financial strain, it doesn't necessarily demonstrate that the in-house option would have been cheaper. As such, BML felt that they should be given the opportunity to look into this further before a conclusion had been reached.

- BML also said that had Mr S taken an Equitable Life in-house AVC, his investment would have been impacted in 2000 when that firm closed to new business, and at the same time, reducing policy payments to plan holders. Therefore, BML say that any remedial action I set should take account of this.

- BML state that in their opinion, given the wording of the consumer's complaint, Mr S has no recollection of the advice provided, whereas the adviser has submitted full details of the advice that they gave, along with his recollections from the time. BML went on to say that the various complaint points that Mr S made were not justified, particularly as, they say, he chose to proceed with the Legal and General FSAVC plan.

- BML said that having thought about the timing of the suitability letter, in their view it was clear from the opening paragraph of that letter, that previous discussions had taken place with Mr S. BML also explained that, had previous conversations not taken place, the adviser wouldn't have needed to caveat the suitability letter relating to previous discussions and correspondence. BML said that, as the adviser and consumer knew one another, it's unlikely in their opinion that the discussion on 28 October 1996 would've been the first time that AVCs had been discussed.

- BML said that further analysis of the Equitable Life AVC offering and its returns should be considered and compared to the Legal and General route that Mr S went down, before a decision is made on the suitability of the FSAVC plan that was arranged. BML said that they don't believe the Legal and General plan has disadvantaged Mr S or that inappropriate advice was provided.

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 carefully considered BML's further submissions and looked closely again at the complaint file. Having thought about what BML have had to say, I'm not persuaded to alter my thinking from what I set out in my provisional decision. I'll explain why below.

BML have said that, as the in-house AVC was provided by a third-party firm who at the time were under financial strain, it doesn't necessarily demonstrate that this route would have been cheaper. I've already acknowledged in my provisional decision that, whilst in most cases the in-house AVC route is typically cheaper, it's not always the case. Importantly though, the regulator at the time required firms to explore in-house charges before deciding whether to progress with an external FSAVC plan, and BML have already conceded that they didn't do this. So, whilst it may subsequently transpire that the external FSAVC plan was a cheaper option, that would only be by accident rather than by good design.

BML have said that in their opinion, greater weight should be placed on the recollections of their adviser rather than Mr S's generalised comments. In reaching my decision, I've carefully considered the submissions of all parties, but we are an evidence-led service and as such, I have to place weight on the written documentation provided to Mr S by BML from the time. Having considered that documentation, it seems clear to me that BML failed to follow the direction that the regulator issued in May 1996, five months prior to their advice (RU20).

Whilst I appreciate that BML have said that Mr S chose to proceed with the Legal and General FSAVC plan, BML weren't just there to transact what Mr S might have thought he wanted. As his adviser, it was their responsibility to consider his full circumstances and ensure that they followed the approach (RU20) which the regulator had clearly set out at the time.

BML have said that it was clear from the opening paragraph of the 1996 suitability letter, that previous discussions had taken place about Mr S's pension planning. BML also said that, as the adviser and consumer knew one another, it's unlikely in their opinion that the discussion on 28 October 1996 would've been the first time that AVCs had been discussed. If Mr S had a friendship with BML's adviser outside of the retirement advice that was provided, I think it's more likely than not that had the adviser recommended Mr S properly explore the in-house AVC, he would've taken heed of that direction because of the friendship.

As I've already explained, BML issued their suitability letter to Mr S on 28 October 1996 – that was the same day that he also signed the FSAVC application form. Whilst BML believe that earlier interactions had likely taken place, there's no evidence available about the content of any such discussions, so I'm limited to the evidence provided and what I think is most likely to have happened from what I've seen. I'm not persuaded that BML held any detailed discussions with Mr S about the availability of in-house AVCs because I think that had they done, it would've been reflected in the letter that they issued to him on 28 October 1996. And as I've already said, their letter suggested that Mr S might want to contact his employer to obtain benefit projections, but importantly, that appeared to relate purely to what his main scheme would likely provide at normal retirement age, rather than the costs of the in-house AVC scheme.

So, whilst BML have said to this service that Mr S was referred back to his company for details of the in-house AVC, I've not seen any evidence to confirm that he was. BML's letter only suggested that he speak to his employer to obtain details of the benefits from his main scheme, rather than the in-house AVC option. So, even had the potential for lower charges been brought to Mr S's attention at the meeting on 28 October 1996, he wouldn't have been in a position to explore that further because BML proceeded with the FSAVC application form the same day.

BML said that further analysis of the Equitable Life AVC offering and its returns should be considered and compared to the Legal and General route, that Mr S went down before a decision is made on the suitability of the FSAVC plan that was arranged. Whilst an analysis may (or may not) demonstrate that Mr S was better off by being placed in the FSAVC, BML's adviser failed to follow the clear regulatory requirements that the PIA had set out at the time.

I've thought about what BML have said about the remedial action that I've set and the fact that it should acknowledge that Mr S's investment would have impacted following the closure of Equitable Life to new business. However, I'm satisfied that the redress I've set adequately caters for this, because 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.

So, for the reasons that I've set out above, I'm upholding Mr S's complaint and require BML to take the actions below to determine whether he has suffered a loss as a consequence of their advice.

Putting things right

BML 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 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, BML 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 Mr S'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 Mr S 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 his 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

I uphold the complaint and require Berkeley Morgan Limited to put things right for Mr S in the manner that I've set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 2 February 2024.

Simon Fox
Ombudsman