DRN-3717672

The complaint

Mr A complains about Scottish Equitable Plc's (Scottish Equitable) decision regarding the alternative fund that his 2016 single premium contribution should have been allocated to, following the closure of one of the funds that it had been erroneously applied to in 2016.

What happened

Mr A has held a pension plan within his employers' group personal pension scheme – administered by Scottish Equitable, since 1999. He made regular contributions alongside his employer and some single contributions. His plan had been set up so that 50% of his investments went into the with-profits (WP) fund and the other 50% was invested across a variety of other funds – which has changed over the term of the plan.

In March 2016 Mr A made a single contribution of over £90,000 which was made in line with his then existing investment strategy.

In December 2020 Mr A wanted to make another single contribution on the same basis as 2016. But Scottish Equitable advised Mr A that, while his regular contributions could continue as before, his intended single contribution was regarded as a new payment. And as the WP fund was now closed to new business the single contribution couldn't be applied to the fund. Scottish Equitable asked Mr A into which fund he'd like his contribution to be invested. He confirmed he would like it allocated to the other fund he was invested in – which was the balanced core fund.

Shortly after Scottish Equitable wrote to Mr A and said that it had made an error in allowing the 2016 contribution – as its WP fund had been closed since 2013. It wanted Mr A to select an alternative fund for his 2016 payment.

But Mr A didn't think that was fair and complained that, as it was him that spotted the error over four years later, it wouldn't be fair to move that contribution from the WP fund. In particular he was concerned about the effect on the bonus he'd accrued. He said it should "*leave things exactly as they are*".

Mr A asked Scottish Equitable a number of questions about the effect this would have on his accrued final bonus, what choice of other available funds he had, and also whether Scottish Equitable would use the 2016 prices of those available funds.

Scottish Equitable confirmed that:

- Mr A could select from the whole of its fund range.
- There would be no loss of accrued bonus from the WP fund.
- Scottish Equitable would carry out a calculation to see if Mr A would have benefited from staying in the WP fund. If it was found that the alternative fund would have benefitted him instead then he would be allowed to keep that gain.
- The number of units that were purchased in 2016 would be invested into the chosen alternative fund using the 2016 prices.

So Mr A nominated an alternative fund, the TEC fund – *for illustrative purposes only*, to establish a comparison of fund values.

In subsequent emails Scottish Equitable confirmed that Mr A would be £141,102 better off as a result of having invested in the TEC fund instead. Following this information Mr A instructed his employer to cease his pension contributions as any additional benefit would take him close to the lifetime allowance. He also instructed Scottish Equitable to switch his funds in line with their agreement.

But Mr A said Scottish Equitable refused to carry out the switch stating the fund value would be "pegged" to the current value of the WP fund. He didn't think that was fair and said it should honour the increased value that had occurred as a result of him selecting the alternative TEC fund.

Subsequently Scottish Equitable said that Mr A could remain invested in the WP fund. It said its calculation showed that he wouldn't be disadvantaged from remaining in the WP fund. It also said that it could resume taking contributions from his employer without any payments being missed. But it paid Mr A £500 compensation for all the inconvenience it had caused during this time.

But Mr A also brought his complaint to us around the same time where one of our investigators looked into the matter. She thought Scottish Equitable should allow Mr A's 2016 investment into the WP fund – as originally requested. She considered the subsequent actions to be "*a series of mistakes*", so she didn't think it was fair to tell Scottish Equitable to honour its offer of investment into the alternative TEC fund. She thought that overall Scottish Equitable's offer of £500 compensation for the distress and inconvenience caused was fair and reasonable.

Mr A didn't agree with the outcome. He said that, while he broadly accepted that his original intention had been to remain in the WP fund, it was Scottish Equitable who had "pressurised" him to nominate an alternative fund. He questioned whether the offer of a back dated valuation of any alternative fund constituted a 'contract' which Scottish Equitable should now honour. He said that the payment of £500 compensation was insufficient when considering the anguish he had suffered over the last nine months.

The investigator wasn't persuaded to change her mind. She said she didn't believe that Scottish Equitable's offer to move to another fund constituted a 'contract' therefore it wasn't bound to honour it. She also said she'd reconsidered Scottish Equitable's £500 payment for the distress and inconvenience Mr A had been caused, but she thought it was in line with what she'd expect for similar situations.

But Mr A didn't accept the position. He said the arrangement with Scottish Equitable met all four requirements of a 'contract' in UK law. He wanted his complaint to be referred to an ombudsman – so it was passed to me for review.

My provisional decision

In my provisional decision I said Mr A's complaint should be upheld. But I said that the 2016 contribution should be applied across the other funds that Mr A's pension was invested in at the time. I said that a *notional* value of investment into those funds should then be compared with the current value of his plan and any loss should be paid into the pension. I made the following points in support of my findings:

- Based on the evidence I'd seen; I was satisfied that Scottish Equitable needed to correct its error and apply the 2016 contribution to a different fund.
- Looking at the options Mr A would have had in 2016, I thought Scottish Equitable's usual approach where a fund had been closed to new investment would have been to nominate a similar fund in profile to the fund that had been closed. But it didn't take that approach when it couldn't accept Mr A's 2020 contribution – so it was difficult to conclude it would have done that in 2016.
- So Mr A would have needed to make that decision himself in 2016 – without the benefit of hindsight which he had in 2020. I thought he might have considered funds with a similar risk profile to the WP fund – but in 2020 he nominated a fund which couldn't be seen as anything other than higher risk.
- So I concluded that the best evidence of what he would done in 2016 was the decision he made in 2020 with his other contribution – which was to invest across the other 50% of funds that he was invested in.
- If Scottish Equitable was unlikely to have provided him with information about alternative, similar funds – and with the need to make a reasonably quick decision, I think that was the most likely choice Mr A would have made in 2016 if he'd been made aware that he couldn't make his contribution into the now closed WP fund.
- I did consider whether to recommend the use of industry type benchmark as a comparison, but I thought that was more appropriate if Mr A had moved to a new provider. The choice he had in 2016 was limited to the range of funds offered by Scottish Equitable so I thought the fairest solution was to try to identify which of these funds he was most likely to have nominated in the circumstances.
- I didn't think Scottish Equitable's offer to allow Mr A to switch to the higher rate TEC fund constituted an "contract" so I didn't think it should have to honour its offer. Nor did I think it was reasonable to recommend that the TEC fund be used, given that Mr A had been able to nominate that fund – with the benefit of hindsight and up to date investment data – and which was outside of the general investment strategy he had previously adopted with his plan.

Responses to my PD

Mr A accepted my redress formula recommendation. But he made the following points in support of his position:

- He had transferred his pension to new provider on 8 October 2021.
- In 2020, when he wanted to invest a new single contribution, he chose to invest into the main alternative fund in his portfolio – not across all his funds. That was because he only held one other fund which represented a small proportion of his overall investments.
- In 2020, when Scottish Equitable asked him to nominate a fund for the retrospective reallocation of his 2016 single premium, he was told that his terminal bonus from the WP fund wouldn't be affected. Therefore he didn't believe the terminal bonus should be included in my redress recommendation.

Scottish Equitable didn't accept my provisional decision and through several submissions made the following points:

- It felt strongly that the outcome it had already implemented – to allow Mr A to remain in the fund he wanted to in 2016, was fair and reasonable.
- It had tried to accommodate Mr A's request to "*leave things as they are*" from December 2020, and its principle of reaching a fair and reasonable outcome which put Mr A back in the position that he would have been (or as close to). It thought the

best option of meeting those options was to leave him invested in the WP fund as he had been since 2016. It also paid Mr A £500 for the distress and inconvenience caused.

- The solution I had proposed based on Mr A's actions in 2020, was to invest in very different funds to the unitised WP fund – where the growth is added through bonuses. And the term of the investment in 2016 would have been significantly different to 2020.
- Mr A had now transferred his pension to another provider which would involve Scottish Equitable having to obtain information from that provider.
- In 2020 Mr A was only invested into one other fund apart from the WP fund – which meant that contribution was directed to the other fund. But in 2016 Mr A was invested into three funds including the WP fund– so it would be difficult to allocate the single contribution on the same basis as 2020, especially as the other two funds aren't equally split as an investment.

Following the information I was provided with, I made both parties aware that I was likely to change the redress formula to ensure any loss was capped at the point Mr A transferred his pension away and then brought up to date.

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.

And having considered the further submissions from both parties I see no reason to depart from my provisional findings, except to include the revision I said I would make to the redress formula. I think Scottish Equitable needs to carry out the calculation I've set out below to see if Mr A has suffered a financial loss here, so I'll set out my reasoning.

<u>*The 2016 contribution*</u>

There's no dispute here that when Mr A wanted to make a single premium contribution to his pension in 2020, he wasn't able to make into one of the two funds he was invested in, as it was closed to "new business." He was asked to make an alternative fund choice – which he did. Subsequently Scottish Equitable echoed the same problem about a contribution he had made in 2016 – which been allocated to the WP fund, although that fund had been closed for new contributions since 2013.

Scottish Equitable asked Mr A to select an alternative fund for that contribution as well but he thought – some four years on – things should be "*left as they are*". But Scottish Equitable remained of the view that the contribution should simply have not been made into what was a closed fund. It explained that, "*as the WP2 fund was closed due to changes in legislation, we must adhere to this. In this case the one off payment was invested incorrectly and we must rectify it."*

Scottish Equitable's position about Mr A's 2020 contribution was that, "*we cannot allow the money you have sent us to be applied to the WP fund."*

So I think Scottish Equitable was firm in its stance, although this subsequently softened when it offered to put things right, that it simply wasn't possible to make a contribution into the WP fund after 2013 and that it would be against legislation to do so. Scottish Equitable doesn't now accept the redress I proposed in my provisional decision because it thinks it's already offered to put Mr A back into the position he ought to have been without its error and that was what Mr A asked it to do.

But if it wasn't possible to make the contribution into the WP fund in 2016 then Mr A's single premium wouldn't now be invested in the WP fund – so that wouldn't put him back as close to the position he would now be in without the error. So that's what I've gone on to consider – the position that Mr A should now be in.

What fund should have been used?

In order to decide how Mr A's 2016 single premium should now be invested, I've looked at his position in 2016 had Scottish Equitable told him that his money couldn't be invested into the WP fund. The first option I believe Mr A ought to have been given was Scottish Equitable's normal position regarding closed funds, as set out in an annual pension statement from April 2016 – which noted "*changes to your policy conditions.*"

This said that, "*any alternative fund that we nominate under 4.4, 5.2 and 6 above will be a fund that we consider closely reflects the make up of the fund that is removed or closed. If you do not want to be invested in the alternative fund chosen by us, then you must give us alternative instructions as detailed in 4.4, 5.2 and 6 above or change your fund after the action mentioned in those conditions has taken place.*"

So I think Scottish Equitable should have nominated a fund that was similar in profile to the WP as an alternative for Mr A in 2016. I think, without giving Mr A advice, it could have furnished him with the information about funds similar to the WP fund. But I note this didn't happen in 2020 when the same situation arose, and Mr A was asked to choose a fund himself – so I can't reasonably say Scottish Equitable wouldn't have done that in 2016 either.

That means Mr A would have had to make the decision himself in 2016 and I think it's reasonable to assume that he would have taken the same approach as he did in 2020 when faced with the same situation – namely that he chose to invest across the other 50% of funds that he was invested in. I now understand that Mr A was only invested in one other fund in 2020 instead of the two other funds he was invested in in 2016. But I don't think that would have affected his decision as I think he would have still taken the same view of investing across the other funds. I think that would seem a reasonable decision for Mr A to have make when he would have been unsure of what other alternative funds to choose from and didn't have the relevant information from Scottish Equitable to help in that respect.

Scottish Equitable has raised the issue of the change in composition of Mr A's funds since 2016 and the difference in the split of each investment. But as I said in my provisional decision, I think the investment would have been made into the same funds, in the same proportion – which I'll confirm in the redress section below. In my view, when confronted with the question of how to invest his single premium in 2016, Mr A would simply have chosen to spread the money across the funds that he was able to invest in within his plan – according to the proportion he was already invested in within each one.

The other possible resolutions

I have taken other possible or proposed resolutions into consideration when making my decision here.
I have carefully considered Scottish Equitable's offer to leave Mr A invested in the WP fund, which satisfied both Mr A's initial suggested solution and also the basic principle of ensuring he remained in the position he had already been in for four years. It also ensured he neither gained an advantage nor was disadvantaged as a result of the offer.

But as Scottish Equitable has consistently said, Mr A simply wasn't allowed to invest his single premium into the WP fund in 2016, so it wouldn't be possible for his single premium to be invested in that fund now. That wouldn't put Mr A into the position he would be now if Scottish Equitable had acted correctly in 2016.

I've also thought about Mr A's request to switch into the TEC fund in 2020 – when Scottish Equitable said that it would allow Mr A to switch to that fund, only to then change its mind and use the WP fund to "peg" a comparison and ensure Mr A didn't suffer a financial disadvantage. But I don't think the discussion between Mr A and Scottish Equitable constituted a "contract" that it needed to it had to honour around the TEC fund, and I don't think it's right to make Scottish Equitable let Mr A pick a fund, with the benefit of significant hindsight, which would be at odds with the general investment strategy he had previously adopted. So I don't think that resolution would be fair or reasonable.

I did also consider whether it would be fair to compare the position of Mr A's plan now with the notional value of his plan using an industry type benchmark in line with his attitude to risk. But I've discounted that option because, while that would be appropriate for a situation where Mr A had transferred his plan to another provider, it's possible to decide here, on balance, what I think Mr A would have done using the range of funds available from Scottish Equitable in 2016.

Putting things right

My aim is that Mr A should be put as closely as possible into the position he would probably now be in if he had been given the correct information in 2016 about how his single contribution had to be invested.

What must Scottish Equitable do?

To compensate Mr A fairly, Scottish Equitable must:

Compare the performance of Mr A's investment with that of the "benchmark" shown below. If the actual value is greater than the fair value, no compensation is payable.

If the fair value is greater than the actual value there is a loss and compensation is payable.

Scottish Equitable should add interest as set out below:

Scottish Equitable should pay into Mr A's pension plan to increase its value by the total amount of the compensation and any interest. The amount paid should allow for the effect of charges and any available tax relief. Compensation should not be paid into the pension plan if it would conflict with any existing protection or allowance.

If Scottish Equitable is unable to pay the total amount into Mr A's pension plan, it should pay that amount direct to him. But had it been possible to pay into the plan, it would have provided a taxable income. Therefore the total amount should be reduced to *notionally* allow for any income tax that would otherwise have been paid. This is an adjustment to ensure the compensation is a fair amount – it isn't a payment of tax to HMRC, so Mr A won't be able to reclaim any of the reduction after compensation is paid.

The *notional* allowance should be calculated using Mr A's actual or expected marginal rate of tax at his selected retirement age.

For example, if Mr A is likely to be a basic rate taxpayer at the selected retirement age, the reduction would equal the current basic rate of tax. However, if Mr A would have been able to take a tax free lump sum, the reduction should be applied to 75% of the compensation.

Scottish Equitable has confirmed it has already paid Mr A £500 for the distress and inconvenience caused by this matter.

Income tax may be payable on any interest paid. If Scottish Equitable deducts income tax from the interest it should tell Mr A how much has been taken off. Scottish Equitable should give Mr A a tax deduction certificate in respect of interest if Mr A asks for one, so he can reclaim the tax on interest from HM Revenue & Customs if appropriate.

Investment name	Status	Benchmark	From ("start date")	To ("end date")	Additional interest
Individual GPPP	Still exists and liquid	The other two funds that Mr A's pension was invested in at the time of the contribution – and allocated according to the underlying percentage proportions of each fund.	Date of 2016 investment	Date that Mr A transferred his pension to another provider bringing any loss up to date using a percentage of loss applied to the current value of the funds.	8% simple per year from final decision to settlement (if not settled within 28 days of the business receiving the complainant's acceptance)

Actual value

This means the actual amount payable from the investment at the end date.

Fair value

This is what the investment would have been worth at the end date had it produced a return using the "benchmark" above.

Any additional sum paid into the investment should be added to the *fair value* calculation from the point in time when it was actually paid in.

Any withdrawal, income or other distributions paid out of the investment should be deducted from the fair value calculation at the point it was actually paid so it ceases to accrue any return in the calculation from that point on. If there is a large number of regular payments, to keep calculations simpler, I'll accept if Scottish Equitable totals all those payments and deducts that figure at the end.

My final decision

I uphold the complaint. My decision is that Scottish Equitable Plc should pay the amount calculated as set out above.
Scottish Equitable Plc should provide details of its calculation to Mr A in a clear, simple format.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 21 December 2022.

Keith Lawrence
Ombudsman