DRN-3769990

The complaint

Mr H complains that Nutmeg Saving and Investment Limited made an error that meant he missed out on his ISA allowance for 2019/2020 for £20,000.

What happened

Mr H holds an investment account with Nutmeg. On 1 April 2020 he asked Nutmeg if the £20,000 he'd deposited would be applied to his stocks and shares ISA before the end of the tax year. He was told that it would. Later he found out that the money had gone into the general investment account rather than his ISA. Nutmeg said that this was because his ISA wasn't set to auto-renew which meant he didn't have an ISA open to put the money into. Nutmeg accepted that it should've spotted this when Mr H was asking and had it done so, the ISA subscription would've been made on time.

Nutmeg calculated redress in line with the approach the Financial Ombudsman Service sets and offered him £1,500 to settle the complaint. Mr H said he's missed out on a lot more than that amount and asked for the Financial Ombudsman Service to investigate.

Whilst our Investigator was considering the complaint there were additional offers made from Nutmeg after considering different calculations to work out the potential Capital Gains Tax (CGT) liability that Mr H may incur from the error. The most recent offer is a total of £7,000.

Mr H didn't accept this offer and asked for an Ombudsman to review the complaint. He said that he intended to hold his ISA for 30 years, and the fund he invested in has historical performance of 8.8% which is the return rate that should be used. Mr H also said that if Nutmeg wanted to reduce the redress in line with inflation, then a rate of 2% should be used. He also felt that he wouldn't have any of his CGT allowance available.

Nutmeg felt that inflation should be applied at a rate of 5.5%. However it said it would accept a rate of 2% but would reduce the return on the investment to 5.74%. It said that it would calculate the loss as if Mr H held his ISA for 20 years rather than 10 years.

Our Investigator felt that the return rate should be 8.8% and the inflation rate applied should be 2.5% and it should be calculated over a 20 year period.

I sent my provisional decision on 13 September 2022 in which I explained I intended to uphold the complaint. I said aside from the term, there was no reason to depart from the Financial Ombudsman Service's usual approach for redress. The relevant extract, which forms part of this decision, is as follows:

"The only thing for me to decide in this case is the financial loss that Mr H has/is likely to incur because of the error Nutmeg has acknowledged it has made. It's not in dispute that Mr H's £20,000 deposit ought to have been protected from tax inside an ISA wrapper. What is in dispute, is how to put things right.

The position that has been put forward by all parties at this point doesn't follow our published guidance. And, aside from the length of time Mr H would've held the investment for, I see no *reason to depart from the guidance. To clarify, the issue that Mr H faces is that any growth of the £20,000 investment he made will now be subject to CGT. Especially because it's clear from the evidence that Mr H is able to, and does, fully fund his ISA allowance each year. This means there isn't space to absorb the £20,000 into his ongoing ISA subscription. In cases like this we make the following assumptions:*

1. *Any charges on holding the investment outside the ISA will not be significantly different from those that would have applied if it had been held within an ISA*
2. *Mr H will pay tax on the investment at the highest rate applicable to him*
3. *Mr H's tax position will remain unchanged for as long as they hold the investment*
4. *The tax position of the investment will remain unchanged while he holds it*
5. *If the investment pays dividend distributions, it will return 7.5% each year (made up of 5% growth and 2.5% dividend)*
6. *If the investment pays interest distributions, it will return 6% each year (made up of 1% growth and 5% interest)*
7. *If the investment doesn't pay either interest or dividends (e.g. growth stocks), it will grow at 7.5% each year*
8. *The investment will be held for 10 years before it is sold.*

In Mr H's case, he's an additional rate tax payer and looking at his job I can't see any reason to suspect that his tax position will change over the next 20 years. And this is the only point that I see fit to depart from the above assumptions.

The redress is to ensure that Mr H doesn't lose out when he sells his investment as if it was inside the ISA wrapper, he wouldn't pay any CGT. Ordinarily we expect investments to be sold after 10 years. However, Mr H is in his thirties and has a senior position at work. I think it's very likely he'd have no reason to cash in his investments for many years to come. Mr H has said he would hold his investments for 30 years. I think this is too long a time period to suggest. I think it's likely that after 20 years, Mr H may be wanting to cash in some of his investments. I do accept that usually we suggest 10 years, but I've not seen anything to show me that Mr H would likely have a need or desire to sell his investments in that timeframe given his age, position and current salary. So, it follows that I think we should use the assumption of 20 years when calculating what he's lost out on in the circumstances of this case.

Other than this I see no reason to depart from our usual approach. I appreciate Mr H has sent evidence showing historic performance of the fund he invests in and this shows 8.8%. But historic performance isn't a guarantee of future performance and we're looking over a very long timescale here. So I don't think it's enough to depart from our usual approach of using a return of 7.5% (5% growth and 2.5% dividend in this particular case). Equally, I've seen nothing to suggest we should be using a lower return rate as put forward by Nutmeg of 5.74%.

There have been multiple debates about inflation, and at what percentage that should be set. But our usual redress has no mention of taking account of inflation, thereby reducing the redress. The method is set to give Mr H a monetary sum that equals the tax benefits he will lose in the future by virtue of Nutmeg's error. What Mr H does with that sum now will enable him to make up any shortfall he thinks he may experience. There's no reason to assume Mr H would use up his CGT allowance in that specific year so I think it's reasonable for Nutmeg to take account of that in its calculations. However, I do think it's likely that Mr H's dividend allowance is used up each year. Mr H has provided us with details of his finances and investments and I think that it's likely he receives dividend payments over and above the £2,000 allowance he's entitled to each year. So, I don't think it would be fair to assume that the dividends he receives from this investment wouldn't be subject to tax.

To summarise, aside from believing that in this case Mr H is likely to not sell his investment for 20 years rather than 10 years, I see no reason to depart from our established approach for redressing his loss of tax benefits. So, I intend to direct Nutmeg to calculate redress on that basis. I can see its original offer was calculated in line with this approach but for the time the investment would be held, so I intend to direct it to do the same with a 20 year investment time period rather than 10.

Putting things right

I intend to direct Nutmeg Saving and Investment Limited to calculate the potential loss that Mr H may incur due to its error which led to £20,000 being held outside of his ISA. To do so Nutmeg should use the following assumptions:

1. *Any charges on holding the investment outside the ISA will not be significantly different from those that would have applied if it had been held within an ISA*
2. *Mr H will pay tax on the investment at the highest rate applicable to him*
3. *Mr H's tax position will remain unchanged for as long as they hold the investment*
4. *The tax position of the investment will remain unchanged while he holds it*
5. *If the investment pays dividend distributions, it will return 7.5% each year (made up of 5% growth and 2.5% dividend)*
6. *If the investment pays interest distributions, it will return 6% each year (made up of 1% growth and 5% interest)*
7. *If the investment doesn't pay either interest or dividends (e.g. growth stocks), it will grow at 7.5% each year*
8. *The investment will be held for 20 years before it is sold which will trigger a CGT liability"*

Responses to the provisional decision

Both parties responded to the decision. Nutmeg provided calculations to show what the total compensation would be. Mr H responded and made the following comments:

- He's explained that he'd have used up his CGT allowance and has passed evidence of his unrealised gains showing these are far beyond the threshold. He's asked the redress be calculated on the basis that his CGT allowance would've been used up.
- He emphasized that he has considerable savings, a healthy salary and wouldn't need access to his funds for at least 30 years, he has asked that the redress is changed to 25 years rather than the 20 years set out in the provisional decision.

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.

Having done so, I've reached the same decision set out in my provisional decision dated 13 September 2022 for the same reasons (relevant extract above which forms part of this decision). I will address Mr H's points and explain why these don't lead me to change my decision.

Firstly, the redress I set out assumed that Mr H would have his CGT allowance available for the year he'd likely realise the gains. I accept that Mr H has a number of investments which have, at this point, made substantial gains. He's provided evidence of significant unrealised gains. But these are unrealised and could change. So it's too speculative to know when Mr H would cash in any of his investments, and he's insisted that he wouldn't need to for some 30 years. I've explained in my decision why I thought 20 years was the fair length of time to assume he'd hold the investments for in this particular case. But I explained it's likely Mr H would want to cash in some investments – so I don't think it's fair to assume he'd realise all his gains over a specific period of time, and in this case it's simply too far in the future to suggest he wouldn't have his CGT allowance available.

We can't know what will happen in the future, and the redress set out in this complaint is based on assumptions. I don't think it would be fair or reasonable to say that Mr H wouldn't have his CGT allowance available in 20 years' time. Mr H has also asked for the term to be extended to 25 years. But as I've mentioned above, it is too speculative to know what will happen over that length of time. I agree that Mr H is in a good position now and will likely not need to cash in his investments for some time. But I don't think it's fair or reasonable to ask Nutmeg to go beyond 20 years when looking to reimburse him for his potential losses as it's too speculative to know what situation Mr H would be in after that period.

As I've not seen anything that changes my decision, I uphold this complaint. Nutmeg is able to assume that Mr H's CGT allowance would be available when calculating redress but must assume that his dividend allowance is taken up each year and therefore any dividends would be taxable as the applicable rate of tax.

Putting things right

I direct Nutmeg Saving and Investment Limited to calculate the potential loss that Mr H may incur due to its error which led to £20,000 being held outside of his ISA. To do so Nutmeg should use the following assumptions:

1. Any charges on holding the investment outside the ISA will not be significantly different from those that would have applied if it had been held within an ISA
2. Mr H will pay tax on the investment at the highest rate applicable to him
3. Mr H's tax position will remain unchanged for as long as they hold the investment
4. The tax position of the investment will remain unchanged while he holds it
5. If the investment pays dividend distributions, it will return 7.5% each year (made up of 5% growth and 2.5% dividend)
6. If the investment pays interest distributions, it will return 6% each year (made up of 1% growth and 5% interest)
7. If the investment doesn't pay either interest or dividends (e.g. growth stocks), it will grow at 7.5% each year
8. The investment will be held for 20 years before it is sold which will trigger a CGT liability

My final decision

I uphold this complaint. Nutmeg Saving and Investment Limited must calculate and pay redress due to Mr H based on the assumptions above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 23 November 2022.

Charlotte Wilson
Ombudsman