DRN-3880588

The complaint

I set out the background to this complaint in my earlier provisional decision, for clarity, I repeat it here.

Mr O complains the level of redress Zurich Assurance ltd (Zurich) have offered following his upheld pension complaint to them is unfair. He doesn't feel it puts him back in the same position had the mistake not occurred.

He'd now like Zurich to increase their offer.

What happened

Mr O originally held a personal pension plan with Sun Alliance, which is now with Phoenix Life. The plan included a guaranteed annuity rate (GAR). In 1993, Zurich advised Mr O to reduce his payments into the Sun Alliance plan and start payments into a replacement Zurich policy.

Mr O complained about that advice in March 2019 and, after reviewing the documentation from the time, Zurich upheld his complaint and determined it wasn't in his best interests to have made those changes given the existence of the GAR.

Mr O took the annuity with the fund that remained at Phoenix when he reached his 65th birthday.

Shortly after his 65th birthday in January 2021, Zurich undertook a loss calculation to establish the impact of the incorrect advice from 1993. They determined that had Mr O remained with Sun Alliance (Phoenix) and maintained his pension payments there, the annuity he received from them would've been £3,482.72 gross per annum higher. Having considered Zurich's assessment, Mr O was satisfied with Zurich's calculation of the shortfall in his pension payments. However, Mr O didn't feel that was enough and wants Zurich to pay him £155,000 to put things right. Having researched the market, Mr O believes it would cost £155,000 to replicate the same benefits he's lost if he were to purchase an annuity himself.

In settlement of his complaint, Zurich offered Mr O a lump sum of £82,491.37 to put things right. In reaching their settlement offer, Zurich looked at the Office for National Statistics data, which suggested Mr O was likely to live until age 85. They then worked out, taking account of investment growth that he could receive on the monies, what they'd need to pay him to replicate those benefits in a single, one-off lump sum. It added this figure to the monthly payments he had already missed out on.

Mr O raised concerns with Zurich about their calculation methodology in February 2021. He told them, in summary, he's unhappy that he's now reliant on the investment returns of a lump sum as, had he remained with the original scheme, he'd have received a guaranteed income for life. He also said, in summary:

- the assumptions used by Zurich were unrealistic and resulted in a lower level of redress than he believes he's entitled to.

- he's unhappy that Zurich have only assumed he'll live until age 85. In doing so, he feels this lessens the redress he believes he's entitled to.

In response to Mr O, Zurich explained their position remained the same. They said it wasn't unreasonable for them to make certain assumptions. They said making such assumptions was commonplace across the financial services industry and they needed to do so to help arrive at what they felt was a fair assessment.

Mr O was unhappy with Zurich's response. He complained to this service setting out the same concerns.

The complaint was then considered by one of our investigators. He concluded that Zurich had treated Mr O fairly. He also said, in summary:

- it was reasonable for Zurich to make the assumptions they did in calculating the redress offered to Mr O.

- the calculations Zurich had provided demonstrated they'd taken account of the 5% annual increase of the lost annuity funds and the solution put forward provided greater flexibility to Mr O than had he taken a single annuity.

Mr O, however, disagreed with our investigator's findings. In summary, he repeated his concerns and said the following:

- It was unreasonable for Zurich to use data from the Office of National Statistics when calculating his life expectancy.

- He believes Zurich should pay him a lump sum of £155,000 rather than the £82,491.37 they've offered. Mr O believes the higher amount would have allowed him to purchase benefits that mirror what he's lost from the Sun Alliance plan.

The investigator was not persuaded to change his view as Mr O did not present any new arguments he'd not already considered or responded to already.

Mr O asked the investigator to pass the case to an Ombudsman to review that outcome.

After carefully considering the dispute, I issued a provisional decision explaining that I planned to uphold Mr O's complaint. After reviewing my provisional decision, Zurich contacted this service and confirmed they accepted my decision. Having considered my provisional decision, Mr O asked for additional clarification on the redress; he explained he still didn't think it was fair because the lump sum Zurich were offering would still be less than that needed to purchase an equivalent annuity.

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.

In my provisional decision, I said that what I didn't think is in any doubt here, is that Zurich were right to uphold Mr O's complaint to them. Zurich have accepted their original advice wasn't right and have tried to put things right with Mr O. What's at the heart of this dispute is whether the solution Zurich have put forward is fair and reasonable.

I've looked closely at the calculations Zurich have undertaken in establishing the income shortfall Mr O has suffered as a result of their incorrect advice. Had he remained with Sun Alliance, the income he received would've amounted to £13,042 p.a. Taking account of the annuity he's now receiving of £6,786 p.a. as well as the annuity he could purchase with the existing Zurich funds of £2,772 p.a., results in an income shortfall of £3,482 p.a. It's this latter amount Zurich have determined needs to be made good and I'm satisfied with that part of their assessment, as is Mr O.

When mistakes occur, it is important consumers are treated fairly when firms look to put things right. Put simply, that means the business must place the customer back into the same position, or as close to the same position they would've been in had the incorrect advice not taken place. We know that as Mr O was advised to divert his premiums away from the Sun Alliance plan and into a Zurich policy, that can't be unwound. So, I need to consider whether the solution proposed by Zurich places Mr O *as close* to the same position he would've been in had the advice to divert his premiums not occurred.

The annuity Mr O received from Sun Alliance is for a single life, with a five-year guarantee providing a 5% escalation that's payable monthly in advance.

In my provisional decision, I also explained there's a number of ways Mr O could be placed back in as close to the same position as possible, the first is via an annuity. That could take the form of either a pension annuity or a purchased life annuity (PLA). Another route would be for Zurich to pay a lump sum to Mr O so he could buy an annuity for himself on the open market. Alternatively, Mr O could be provided with a capital lump sum from which to draw down income payments. Zurich have offered Mr O the latter option, deriving the lump sum from its own assumptions. However, Mr O wants £155,000 so he can go out and buy his own annuity.

Zurich have discounted purchasing a pension annuity for Mr O. They're of the view that doing so would result in a loss of enhanced protection and impact his annual allowance too. This isn't unreasonable; purchasing a pension annuity in this way would involve a significant, one-off, contribution. We wouldn't expect a business to disadvantage someone in this way so I don't think Zurich is in the wrong in rejecting that approach in this respect.

So, I've thought carefully about whether Zurich should buy Mr O a PLA instead or whether it's acceptable for them to offer him a lump sum from which to draw an income in lieu of that annuity. I've also considered whether Zurich should give Mr O a lump sum so he can go out and buy his own annuity. Having thought carefully about this, I'm not convinced providing Mr O with a lump sum to allow him to purchase his own annuity is the right solution. That's because we're compensating him for a regular income until death which a PLA would immediately achieve.

I've looked closely at Zurich's original offer. It's been necessary for Zurich to make a number of assumptions when reaching a final redress capital sum. One of those is Mr O's likely lifespan which Zurich have determined is 85 years old. They've reached that age by reference to the Office of National Statistics website. After taking account of the 5% escalation Mr O would've received had he stayed with Sun Alliance, Zurich have then discounted the final lump sum back to take account of an assumed annual investment return of 1% he could receive if he invested the pot.

I'm not convinced by Mr O's arguments that it's unfair of Zurich to utilize the ONS assumed longevity calculator. The ONS is independent from Zurich and I believe it's necessary for

Zurich to have an informed end point to which their calculations would need to be based on. In addition, when pricing annuities, product providers also need to rely on such data so, in my view, I don't believe Zurich have deviated from common industry practice on this point.

I'm also not persuaded by Mr O's arguments about Zurich's use of the 1% discount / return factor. I believe they've been conservative in nature and, based on a cautious/ low risk rate of return, I'm of the view that approach is reasonable.

The redress payment proposed by Zurich already takes account of the 20% income tax that Mr O would have had to pay had he remained with Sun Alliance and taken the annuity so the payment will be net in Mr O's hands. This'll replicate how the benefit would be taxed had it stayed with Sun Alliance.

Allied to this, I should note that in their calculations, Zurich have assumed that Mr O's existing Appropriate Personal Pension plan with them would yield £22 per £1,000 in income. I well suspect that, if he were to exercise the open market option on that policy now, it would result in a much higher income, particularly given the recent improvements to annuity rates over recent weeks. I understand from Zurich that Mr O has not yet crystalised that policy.

The lump sum payment would offer Mr O the flexibility to vary the income he draws either in the early or later years and I'm satisfied Zurich's assumptions have been modest in nature too. Allied to this, as Mr O is married, the lump sum would provide death benefits for his spouse, even after the 5th year which the annuity would not. From what I've seen, the solution put forward by Zurich would enable him to replace the lost benefits from the Sun Alliance plan. Whilst I accept it's not necessarily in an identical format it is a fair and reasonable alternative.

I've thought carefully about whether Zurich should buy Mr O a PLA instead. I don't think Mr O is being unreasonable in expecting Zurich to replicate the fixed income he's lost as a result of their error. However, I also don't think Zurich has been unfair or unreasonable either in the approach they've taken to try and put things right. It has offered a cash sum to sort out the complaint quickly and informally, and the assumptions they've used look plausible. Broadly that cash sum is about right to compensate Mr O. So, it wouldn't necessarily be fair and reasonable to rip things up and start again. However, it's important to recognise that if Mr O does outlive the ONS anticipated mortality age or, if the assumptions Zurich have used prove to be incorrect, Mr O may end up worse off. Whilst I do agree with Zurich in so much as I think it unreasonable for them to purchase a pension annuity, a PLA is an alternate solution to this and the file is silent on whether this was even explored as a possible solution with Mr O. It therefore follows that I'm upholding Mr O's complaint and will ask Zurich to offer Mr O two options; either buy him a PLA to replicate his lost income (with an appropriate level of compensation for the income he has already missed out on) or offer Mr O a cash sum in line with its original approach albeit amended to bring it up to date. In this way, Mr O has a choice and his concerns about Zurich's assumptions and about outliving his capital sum are catered for.

After receiving my provisional decision, Mr O again explained he felt the calculation approach Zurich was adopting was unfair because their lump sum wouldn't match that needed to purchase an equivalent annuity. However, I explained to Mr O that I didn't agree with his perspective because included within the typical purchase cost of an annuity, a provider would include their wider associated expenses such as marketing, IT and administration which, Zurich wouldn't incur by directly paying Mr O a lump sum. Allied to that, as I've already explained above, the lump sum works in a different way in generating the replacement income compared to the annuity. In addition, should Mr O decide he wished to accept the PLA in settlement of his complaint, the purchase price of that is for Zurich to bear, so that cost is inconsequential to him. So, as there is no new information to consider it follows that I have reached the same conclusions for the same reasons as I did in my provisional decision, the details of which I have set out above and I therefore require Zurich to put things right in the manner I've set out below.

Putting things right

A fair and reasonable outcome would be for Zurich to put Mr O, as far as possible, into the position he would now be in had it not been for their error.

As I've already said, I think Zurich's original approach was acceptable albeit it didn't address Mr O's original desire for a *guaranteed* income for life. Taking that into account and given the passage of time that's now elapsed, I believe Zurich should give Mr O a choice of how things should be put right: the flexibility of a lump sum payment which provides the opportunity to vary the income he receives and leaves a legacy on death, as Zurich have already offered, or the option of buying a purchased life annuity for him that replicates the lost benefits.

Approach 1: As some time has now elapsed since Zurich undertook their loss calculation, they must revisit their approach to update their original settlement offer of £82,491.37. This should take account of payments that Mr O would have received but, to date, hasn't. It should also take account of the fewer future annuity payments that now need to be made. Zurich can use the same assumptions as previously and should use the date of settlement as their end point.

Approach 2: Alternatively, if Mr O would prefer, Zurich should offer to buy Mr O a single life PLA, with a five-year guarantee providing a 5% escalation that's payable monthly in advance. The PLA should match the same income he would have obtained from the Sun Alliance plan, £3,482.72 gross, per annum.

Under either approach, Zurich must account for the annuity payments Mr O has missed out on. It should do this as follows:

- Zurich must work out how many income payments Mr O has not received since his 65th birthday to the date of settlement.
- Zurich should then add 8% simple interest from the date each amount should have been paid to the date of actual payment and pay this amount to Mr O.

Where interest is being added at 8% simple per annum, this is likely to be subject to tax applied by HM Revenue & Customs. If Zurich deducts tax, it should tell Mr O how much it has taken off. It should also give Mr O a certificate showing this, if requested by Mr O so he may reclaim the tax from HM Revenue & Customs, if appropriate.

Zurich must write to Mr O setting out the revised calculations and options in a simple, easy to understand format.

My final decision

I uphold this complaint and require Zurich Assurance Ltd to pay Mr O the compensation amount as set out in the steps above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr O to accept or reject my decision before 24 February 2023.

Simon Fox
Ombudsman