DRN-4071865

The complaint

Mr L says Aviva Life & Pensions UK Limited ('Aviva') misled his application for payment from his Aviva Pension Plan ('APP') in late 2021. He mainly claims as follows:

- That Aviva misled him (and his adviser) to believe the entire APP could be withdrawn as a tax-free lump sum, which resulted in him applying for such a withdrawal. However, only 25% of the withdrawal was tax free, the remainder was an Uncrystallised Funds Pension Lump Sum ('UFPLS') payment that was taxable one-off income.

- That Aviva failed to stop the withdrawal despite the obvious disparity between the wholly tax-free payment he had applied for and the majority taxed payment that was processed.

- That the matter resulted in a significant tax liability on him, which would not have happened but for Aviva's error. He would have limited his application to the 25% tax-free element only if he was properly informed.

- That the matter also resulted in loss of a Guaranteed Annuity Rate ('GAR') option because of the withdrawal and in the exhaustion of his Money Purchase Annual Allowance ('MPAA') for the 2021/22 tax year, which prevented him from contributing into another plan in order to mitigate the situation.

- That he should be compensated for his losses and for the stress and inconvenience caused to him.

What happened

One of our investigators looked into the complaint and issued two views on it. Both views upheld the complaint. The second addressed additional information from Aviva and both parties' comments after the first.

Overall, the investigator mainly found that Aviva's initial illustration to Mr L in August 2021 contained the error, in which the entire APP's value was described as tax-free; a statement for the APP in November 2021 updated its value; Mr L and his adviser applied for payment of the APP's full value in the same month; there is evidence that, internally, Aviva noted the error on 15 December 2021, but it then spoke to Mr L on the same date and whilst it told him the tax-free status of the payment had to be checked it also told him it could see no reason why it was not correct; on 17 December 2021 both sides spoke again and this time Aviva informed him about the error (that the APP's value had tax-free and taxable elements); a revised quotation (setting out the tax-free and taxable elements of the APP) was sent to him on 20 December but he says he did not receive it; both parties then spoke again on 29 December 2021, during which Mr L's statements showed he still believed all of the APP's value could be withdrawn tax-free and, in response, Aviva did not correct him; then on 13 January 2022 the payment to him (including tax-free and taxable elements) was confirmed.

The investigator concluded that Mr L had initially been misled by the first illustration; the

telephone call on 17 December then notified him of the error but he does not appear to have properly understood its implications; he says he did not receive the revised quotation; in his last conversation with Aviva (before the payment) he repeated his misunderstanding that the payment was completely tax-free and Aviva did not correct him; there is evidence from Aviva's internal process that it set itself a requirement to verify that Mr L wished to proceed with the payment on the correct basis, but it never conducted this verification; it ought to have done so before making the payment; and because it did not do that the payment was made.

For these reasons the investigator upheld the complaint. After the second view, Aviva agreed with the investigator's findings on merit and redress (and compensation). However, Mr L's adviser said he considered the findings on redress and compensation to be inadequate. The investigator had mainly found that:

- Aviva's offer to Mr L of £300 compensation for the trouble and inconvenience caused to him is insufficient. Instead, an award of £500 for this would be fair. The shock of a tax liability he did not expect would have caused an impact upon him. This would have been compounded by learning it had resulted from an error in the first instance and by the loss of capacity in his MPAA. The overall situation would have taken extra effort to address. Balanced with the fact that Mr L benefited from an adviser's assistance at the time, which would have lessened the impact, an award of £500 for trouble and inconvenience is fair and reasonable.

- Redress for Mr L's tax liability cannot fairly be the refund (of tax paid) that he seeks.

- He has said, but for Aviva's error, he would have withdrawn only the tax-free 25% value from the APP and left the remainder invested; that he would not have needed any more from the APP for some time because he had access to £20,000 in savings and more than that amount in tax-free cash in another policy; and that, in retirement, he needed £1,100 per month income in addition to his state pension and would be able to meet this through his cash balances for up to four years.

- In this context, and given his state pension income, if he withdrew only the tax-free 25% value from the APP any subsequent and future drawdown from the remainder would have attracted tax at his marginal rate of 20%. As such, it was always to be taxed and a refund of the tax he paid because of the full withdrawal would put him in a better position, which is not a fair outcome.

- Instead, fair redress is the difference between the tax he paid because of the full withdrawal (in the 2021/22 tax year) and the tax he would likely have paid on future withdrawals of/from the remainder value of the APP if he had liquidated only the 25% tax-free cash.

- It is impossible to know when the future withdrawals would have been made and what the future value(s) of the remainder of the APP would be, so calculation of redress will need some assumptions and should be as follows – begin with the tax-free cash Mr L could have withdrawn from the APP at the outset; deduct that from its full value; assume that over time the remainder value would have been subject to 20% tax upon withdrawals; calculate that tax (which should result in £5,594.92); deduct £5,594.92 from the £10,863.36 tax liability he actually incurred because of the full payment; the difference of £5,268.44 will be the excess tax he paid and will be the amount Aviva should pay him as redress; there is a matter of a £1,866.96 tax rebate he received in the 2021/22 tax year, if this relates to the APP pay-out it should be reflected in the calculations; and no interest should apply to the redress amount

because it is money that would have remained invested in the APP, not money that would have been available to Mr L.

Mr L's adviser's comments, and the investigator's replies, were mainly as follows:

- He does not consider that £500 is enough to address the trouble and inconvenience the matter has caused him. However, he understands our service could be limited in terms of what we can award him in this respect. In response, the investigator retained the finding that £500 is fair.

- He had a personal allowance with capacity to cover annual withdrawals (through Flexible Access Drawdowns) from the APP of £1,570 without triggering an income tax liability. This would have happened over the four years mentioned by the investigator and it was common for the adviser to make arrangements like this for clients like him in order to provide additional tax-free funds during each tax year. This scenario, and the reduced tax liability within it, ought to be reflected in the calculation of tax he would have paid for future withdrawals. In response, the investigator said this submission conflicts with Mr L's and his adviser's earlier assertion that he had access to alternative funds and would not have had a need to use the APP's funds for four years.

- After the fourth year, some capacity will remain (and continue) within his personal allowance to cover around £1,200 of the additional £13,200 per year he would need to withdraw to augment his state pension. This scenario, and the reduced tax liability within it, also needs to be reflected in the calculation of tax on future withdrawals. In response, the investigator repeated that this too conflicts with his earlier assertion about what would have happened if the APP's full value had not been withdrawn.

- It is unfair not to apply either interest or performance to the APP's remainder value in the calculations. Interest can be justified on the argument that Mr L would have had access to that value through drawdowns, so interest compensates for being denied that access. Performance can be justified on the basis that the remainder would have been invested and would have had investment performance. There is evidence of how the investment in another pension policy he held has performed to the level of 10.46% per year since inception, with a four-year return (up to 2022) of 35.55%. In response, the investigator said that with regards to interest it was Mr L's claim that but for the erroneous full withdrawal he would not have accessed the remainder of the APP after taking the tax-free element. With regards to performance, the investigator said there are conflicting accounts of what would have happened with the APP, but for the full withdrawal, and it is impossible to know what Mr L's future actions would have been in terms of investment within it, and impossible to know whether (or not) any such investment would have performed with growth or at a loss. Hence the assumption, for the calculation, that the APP's value would remain the same.

- He would counter propose settlement of his complaint on the terms of £7,250 in redress and the £500 award for trouble and inconvenience. In response, the investigator noted that the redress counter proposal was not backed by a calculation.

The matter was referred to an Ombudsman.

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.

Aviva has accepted the investigator's finding of its liability in the complaint. I have reviewed the complaint's merits and I agree with this finding and with the key point (in its support) made by the investigator – a point which also complements one of the key arguments Mr L put forward.

Evidence shows there was a clear mismatch between the payment he applied for in November 2021 and the payment made to him in January 2022. He applied for full payment of the APP's value as a completely tax-free payment, yet the payment that was processed and made included both tax-free and taxable elements. His application was informed by the erroneous illustration from Aviva in August 2021. His adviser's covering letter of 9 November 2021, which was submitted with the application form, asked for a completely tax-free payment. The application form itself includes annotation that refers to "ALL TAX FREE" [followed by a word I cannot make out]. The application was never revised. As Mr L says, Aviva made the payment without ever formally reconciling the mismatch. As the investigator said, it failed to uphold the requirement it had noted for itself to do so prior to payment (that is, to verify that Mr L wanted the part tax-free and part taxable payment before it was made).

There is evidence that the error was brought to Mr L's attention (on 17 December) after his application but before the payment was made. I have also noted an argument Aviva previously made about his adviser's responsibility in the matter. However, ultimately it was its mishandling of the process that allowed the payment to be made without confirmation and verification that he agreed with the very important change of condition for the payment. This ought to have been avoided. Especially as his application was explicitly made on the grounds that the entire payment was to be tax-free, and especially after the last conversation with him in December 2021, whereby despite having been told about the error in the preceding conversation he continued to refer to an expectation of a full tax-free payment – and was not corrected by Aviva. Overall and on balance, I consider Aviva's liability for the payment, and for the tax consequences to Mr L arising from the payment, to be well founded. The latter (tax liability) would not have happened but for the former (payment).

Mr L appears to have accepted the investigator's finding that £500 should be awarded to him for the trouble and inconvenience the complaint matter has caused him. I consider that he has accepted this finding, albeit reluctantly, because he used the same amount in his counter proposal for settlement.

I have reviewed the award and I too find it to be reasonable in the circumstances of his case. My consideration has been balanced by reflection of the opportunity he had – but missed – to mitigate his experience by taking proper notice of and/or advice on information about the error he was given on 17 December. The same applies to the fact that impact, from the experience, upon him would have been reduced by his adviser's assistance during the process. It is also my view that an award of £500 extends to covering the effect of losing capacity in his MPAA at the time. I would extend this further to cover any upset caused to Mr L in losing the potential GAR option following the full withdrawal – there is a lack of evidence to support a quantifiable financial loss in this respect, so the matter of upset caused appears to be the limit. Overall and on balance, £500 is a fair and reasonable award for the net effect of the trouble and upset caused to Mr L in the circumstances of his case.

Aviva accepts responsibility to redress the tax liability issue and it does so on the grounds and calculations set out by the investigator. Mr L disagrees with those grounds and calculations.

Aviva's letter to Mr L of 13 January 2022 confirmed the following – the APP's value was £37,299.50; its taxable part was £27,974.62 and the tax deducted from that was £10,863.36;

so, the net payment to him was £26,436.14.

From his perspective, I can understand why Mr L would simply ask for coverage of the tax he incurred. However, the subject matter is essentially the *taxable* element of his APP. In other words, in the absence of evidence that this element would eventually have been accessed in a way that completely avoided tax, the implication is that tax would always have been applicable to any future partial or full withdrawal from it.

If Mr L withdrew only the tax-free payment from the APP, there is no evidence of an arrangement in which future withdrawal of all its remainder value (either over time or at once) was planned to happen without triggering a tax liability. At best, and as I summarised in the previous section, his argument is that those withdrawals would have happened with a lower tax liability than the investigator assumed.

As the investigator noted, this argument conflicts with the claims initially made in support of his complaint. In his initial complaint letter, he said that had he known about the taxable element in the payment he would not have opted for it, and that he would have limited his application to the tax-free element only, "… *and not drawn any income at all*".

In correspondence with Mr L's adviser, the investigator probed further into this issue. His adviser repeatedly confirmed a scenario in which, had he withdrawn only the tax-free payment, Mr L did not intend to draw further from the APP, had no need to do so and would not have done so. The sum of his submissions, some of which were repeated during the correspondence, was that Mr L needed £24,000 per year in retirement, £11,000 (per year) of this was to be derived from his state pension, the remainder was to be derived from the total cash reserves (cash holdings and tax-free drawings from another pension) he had at the time, this would have sustained him for up to around four years, and there was no planned future expenditure at the time that caused a foreseeable need to draw from the APP.

The above serves as reasonable grounds to conclude that, based on payment of the tax-free element of the APP (only), the remainder value in Mr L's APP would have remained as it was and untouched for around four years. The arguments made in his objection to the investigator's redress findings go against the earlier claims. The alternative claim is now that there would have been a need for Mr L to draw from the APP (within his personal allowance) throughout the four years and thereafter, and that he would have done so.

At worst, these contradicting accounts – one without qualification that avoids conflict with the other – suggest that neither is reliable. They could also suggest that only the initial account is reliable and that the subsequent one has mainly been a reaction to the investigator's view on redress. On balance, I am persuaded that the initial account, alone, is reliable. It was given freely and it was repeated/endorsed to us by Mr L and his adviser. It was also broadly consistently maintained up to around the investigator's first view. Furthermore, his adviser's argument about the application of investment performance to the calculation of redress appears to be much more committed than the argument for interest based on access to funds – which suggests an acknowledgement on Mr L's part that the APP would probably have remained untouched, as opposed to being liquidated.

For the above reasons, I do not accept that there are grounds to consider interest in the calculation of redress; and I do not accept that some of the taxable remainder value in the APP (assuming only the tax-free element had been drawn) could have been accessed without triggering a tax liability; instead I consider that drawings from the remainder value would probably have been deferred for around four years, then thereafter any such drawings would probably have been subject to income tax (at Mr L's marginal rate, 20%).

The next issues to address are investment performance and the tax rebate Mr L received

around June 2022.

Mr L's argument for reflection of investment performance in the calculation of redress is not unreasonable. After all, what I have addressed above concludes that the taxable remainder of the APP would probably have remained invested. This naturally couples the notion of investment performance. However, key unknowns prevent such a consideration in his case. It is unclear, and it cannot safely be assumed, what the investment term would have been before all value was withdrawn from the APP. It is also unclear, and it also cannot be safely assumed, what the changing capital amounts (on which performance would need to be calculated) would be over the [unknown] investment term given the probability that after around four years withdrawals from the APP would probably have been made.

Put slightly differently – performance cannot safely be calculated without knowing the amount(s) and timings of probable withdrawals from the APP around four years after 2021/22; that means we cannot know what capital would have remained invested after such withdrawals; and the same applies to the fact that we cannot know the period of time over which the different capital remainder amounts would have continued to be invested. These are broadly the same difficulties the investigator expressed. There is no reliable evidence to resolve them. Nevertheless, a value for the APP (after withdrawal of the tax-free element) must still be used to calculate what would have been Mr L's tax liability over time. For that purpose, and as a compromise in the circumstances, I consider it broadly fair and reasonable to assume the same value it had at the point of payment in January 2022.

With regards to the tax rebate, the investigator suggested that clarification should be sought on whether (or not) the rebate was connected to the payment from the APP. There appears to be evidence from Mr L's adviser suggesting that the rebate was directly connected to that payment. In email correspondence with us on 20 December 2022 a copy of the HMRC rebate related letter was shared, as was his P45 for the 2021/22 year. The adviser's description of information about the rebate was as follows –

"*This should confirm the refund by HMRC of £1,866.96 in June/July 2022 was in respect to the overtaxing of the Aviva payment. So, of the total income tax paid to HMRC by Aviva ((£10,863.36), the sum of £1,866.96 has been repaid to* [Mr L] *by HMRC*".

Putting things right

I have explained, above, the reasons behind the redress and compensation that I will award Mr L and will order Aviva to calculate and pay to him. In this section, I set out the relevant orders to Aviva. Mr L is also ordered to engage meaningfully and co-operatively with Aviva to provide it with information and documentation he has that is relevant to its calculation of redress and needed to settle redress, and that it does not already have.

To compensate Mr L fairly, Aviva must do as follows:

- Pay him £500 for the trouble and inconvenience the complaint matter has caused him.

- He paid £10,863.36 in tax on the taxable element of the APP payment he received in January 2022.

  The payment statement shows that this arose from the taxable part of the APP valued at £27,974.62. As I treated above, this taxable part of the APP would have remained as it was but for Aviva's erroneous payment. It is to be assumed that the same value would exist when the Mr L would have withdrawn it, over time or at once, in the future. The withdrawal(s) would probably have been subject to income tax at

his marginal rate of 20%, so he would have paid 20% of £27,974.62 income tax. As such, but for Aviva's erroneous payment, he would have paid £5,594.92 income tax on the taxable element of the APP.

The difference between the £10,863.36 tax he paid because of Aviva's erroneous payment and the £5,594.92 tax he would probably have paid without that erroneous payment is £5,268.44. This is 'A'.

Available evidence suggests that £1,866.96 out of the £10,863.36 tax payment was rebated and refunded to Mr L. If his now disputes this both parties (perhaps with any possible assistance from HMRC) must engage with each other in order to establish whether (or not) the rebate was connected to the Aviva payment. Otherwise, and if he stands by his adviser's earlier admission of the connection (as I quoted in the previous section) the rebate amount must be deducted from A. The result is £3,401.48. This is 'B'.

If the tax rebate received by Mr L was connected to the Aviva payment, Aviva must pay him B in redress. If the tax rebate was not connected to the Aviva payment, Aviva must pay him A in redress.

Redress must be accurately based on the income tax Mr L would have paid on the taxable element of the APP in the scenario (and assumptions) that I have set out in this decision and in this section. If, in this context and with relevant information from HMRC and/or upon a redress calculation by an actuary (if the parities choose and agree to use one) the correct and relevant figures differ to what I have stated above, such correct and relevant figures should be reflected instead. Otherwise, what I have stated above must be applied.

My final decision

For the reasons given above, I uphold Mr L's complaint. I order Aviva Life & Pensions UK Limited to calculate and pay him compensation and redress as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr L to accept or reject my decision before 15 June 2023.

Roy Kuku
Ombudsman