DRN-4295002

The complaint

Mr I has complained that Pension Insurance Corporation plc (PIC) provided him with misleading valuations on the annual pension he would receive if he deferred his retirement date.

What happened

The background to this complaint and my initial conclusions were set out in my provisional decision, which I issued last month.

My provisional decision said:

What happened

Mr I was a member of a defined benefit pension scheme provided by his employer. He left pensionable service with the employer in 2000. In 2018 PIC bought out the pension scheme, so they were then responsible for providing Mr I with his pension income when he reached the scheme retirement age. Mr I would receive his pension through a deferred annuity held with PIC.

Mr I was sent a policy schedule which set out details of the deferred annuity held with PIC. This schedule said that Mr I's normal retirement age under the scheme was 60 and that he could expect to receive a pension of approximately £40,000 a year at that age.

Mr I reached his 60th birthday in March 2019. By then Mr I was living in Germany. Mr I said that as the state pension age in Germany is age 63, he decided to delay taking his PIC pension until he was 63, to tie in with when he would start to receive his German state pension.

In December 2019 Mr I asked for details of what pension he could expect to receive if he started to draw his pension in either March 2020 or March 2022.

PIC sent two covering letters with enclosures to Mr I in December 2019. One letter enclosed an estimate of pension benefits at March 2020, the other at March 2022. Aside from these different years, all other wording in the covering letters was identical.

The covering letters stated that: "The figures we quote are estimates based on current factors and we will need to recalculate your final benefits at your actual retirement date."

Together with each covering letter was a document headed "Estimated Retirement Quotation". One quotation set out details of the estimated pension benefits that Mr I could receive if he retired in March 2020. This quoted a total pension of approximately £42,000 a year.

The other quotation set out details of the estimated pension benefits that Mr I could receive in March 2022. This quoted a total pension of approximately £48,000.

In June 2021 Mr I obtained a further quotation from PIC. This was also prepared on the basis that Mr I retired in March 2022 and again quoted an estimated total pension of approximately £48,000 a year.

In October 2021 Mr I did retire and started to receive his pension from PIC. He received confirmation from PIC that he would receive a yearly pension of approximately £42,900.

This figure was less than Mr I had been expecting. He wrote to PIC to ask why his pension was so much less than the March 2022 estimated pension shown in the quotation that PIC had sent to him.

PIC replied to Mr I explaining how they had calculated his pension in October 2021. PIC said that they calculated what the yearly increase would've been in Mr I's pension had he retired at age 60. Mr I's pension at age 60 was approximately £40,000 a year. This pension would've increased in line with the Retail Prices Index (RPI) each year. This annual increase was not capped.

Mr I's pension would increase in January each year following his retirement. Therefore, if Mr I had retired in March 2019, then the first increase in his pension would have been in January 2020.

The annual RPI rate used to calculate the increase in Mr I's pension every January is the rate published in November from the previous year. This would mean that the pension increase calculated in January 2020 would be based on the published RPI rate from November 2019, and so on.

The first increase applied to Mr I's pension would be prorated as he would not have been retired for a whole year at that point. It would be based on the number of whole months between when Mr I retired and the first January following his retirement.

Information provided by PIC show that Mr I's pension increased by 1.7% for 2019 and by 0.9% for 2020. These increases added approximately an extra £1,000 a year to the pension that Mr I would've received at age 60. PIC therefore added approximately £1,000 to Mr I's pension in October 2021, to increase his pension from £40,000 to approximately £41,000.

PIC went on to explain that as Mr I had delayed his retirement by approximately 2 and a half years, they recognised that he had not received any pension income over this period. To reflect this they apply a "late retirement re-spread factor" (LRRF) to Mr I's pension.

PIC have said that the purpose of the LRRF is to re-spread the missed pension that would have been paid to Mr I if he had retired at age 60 over the remainder of Mr I's lifetime. They have further explained that Mr I's missed pension payments were rolled up to October 2021 together with interest to increase Mr I's pension at October 2021. A "re-spread factor" is then applied by PIC to calculate the additional pension payable.

PIC have further explained that "The factor is calculated with a view to provide fair value taking into account future pension escalations, along with any contingent spouse benefit payable. Life expectancy is one of the factors taken into account, but not the only factor. The factor is updated monthly to reflect the current market conditions at the point the benefits are put into payment".

The application of the LRRF by PIC, based on their calculations, added approximately a further £1,900 a year to Mr I's pension in October 2021.

Therefore, as Mr I's pension at age 60 was approximately £40,000 a year, by delaying taking his pension to October 2021, his pension increased by approximately £1,000 a year due to RPI and approximately £1,900 a year due to the LRRF. This gave Mr I his pension of approximately £42,900 a year in October 2021.

PIC further explained that the RPI increase applied to Mr I's pension in January 2022 was also prorated. PIC have said that this was because Mr I started to receive his pension in October 2021, the increase applied to his pension in January 2022 would be based on the number of whole months that Mr I had been receiving his pension in 2021, and not the whole year.

Mr I did not accept PIC's explanation and he complained to PIC. Mr I maintains that the increase in his pension of £2,900 a year whilst it was deferred between March 2019 and October 2021 is lower than the increase he had expected based on the retirement quotations he'd received from PIC. Mr I has also asked PIC for details of the calculations used in the LRRF.

PIC rejected Mr I's complaint. PIC have said that the increases to Mr I's pension whilst in deferment have been calculated and applied correctly. They also said that the additional pension of approximately £2,900 a year that Mr I now receives will increase in line with RPI each year, along with the rest of his yearly pension.

PIC declined to disclose full details of the LRRF calculations to Mr I. They say that their calculations are commercially sensitive information. Whilst PIC didn't uphold Mr I's complaint, they did offer Mr I a good will payment of £50 in consideration of any confusion caused by their retirement quotations.

Mr I brought his complaint to the Financial Ombudsman Service. One of our Investigators considered Mr I's complaint and concluded that the complaint should be upheld. This was because they thought the retirement quotations didn't include all the relevant information that they should have and that this gave Mr I a false expectation. The Investigator concluded that PIC should pay Mr I £150 for the confusion and disappointment this has caused him.

Mr I has not accepted the Investigator's view. Mr I thinks that he should receive a greater increase in his deferred pension and that PIC should disclose full details of their LRRF calculations to him. Mr I asked for his complaint to be referred to an Ombudsman. The matter has therefore been brought to me to consider.

What I've provisionally 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.

Mr I has said that although he could have started to receive his PIC pension in March 2019, when he reached age 60, he had planned instead to retire at age 63, which was in March 2022. Mr I said this was because he had moved to live in Germany, and age 63 was the earliest state retirement age in Germany.

Mr I received late retirement quotations from PIC in December 2019, and again in June 2021. These quotations were all produced by PIC after Mr I's 60th birthday. He received quotations for retirement in March 2022, in line with Mr I's plan to retire at age 63. I have not seen any evidence to show if Mr I received or requested any late retirement quotations before his 60th birthday.

Based on the documents that I have seen it seems reasonable to me that Mr I had decided ahead of reaching age 60 that he would defer taking his pension from PIC until age 63.

I therefore do not think that the retirement quotations produced by PIC had an influence upon Mr I's decision not to start receiving his pension at age 60.

I do however think it likely that on reading the retirement quotations produced in December 2019 and June 2021 they would have had an influence on Mr I's decision to continue with deferring taking his PIC pension.

Mr I had asked for retirement quotations to be produced assuming a retirement age of 63, that is in March 2022. These quotations showed a pension of approximately £48,000 a year.

Mr I decided to take his pension in October 2021, so approximately 5 months before his 63rd birthday. Mr I has questioned the basis on which his yearly pension of approximately £42,900 was calculated when he retired in October 2021.

Following PIC's buyout of the defined benefit scheme, Mr I received a new policy schedule from PIC setting out the terms for his deferred annuity. Paragraph 2.4.2 of this policy schedule, in section 2.4 headed "Adjustment on retirement after Normal Retirement Age" explains the rules on late retirement. This rule states the following:

"The amount of the Member's Scheme Annuity will be adjusted by a late retirement factor. If the Annuity starts after the date on which the Member reaches Normal Retirement Age, that part of the Annuity (if any) will be increased for late payment in respect of the period between the date on which the Member reached Normal Retirement Age and the date the Annuity started being paid. The late retirement adjustment shall be determined as follows:

(a) in respect of the period on and from Normal Retirement Age, the Member's Scheme Annuity shall be adjusted by PIC using its Standard Terms."

No further explanation of what these "Standard Terms" is given. Essentially the policy schedule only says that by deferring taking his pension, Mr I's pension would be increased. But it's not clear in what way exactly. And the retirement illustrations that PIC sent also informed Mr I that he would be receiving more annual pension by deferring taking his pension.

PIC would not disclose their LFFR calculation to Mr I or to this service. In response to my request PIC have said "In terms of revaluation up to Normal Retirement Date we use a future assumption of 2.5%pa for RPI and 1.5%pa for CPI, from Normal Retirement to Late retirement, we assume future increases of 4%/5%/7% per annum depending on the tranche. This is the approach that was agreed with the Trustee during transition for any projected retirement quotations. We use best estimate assumptions re economic and demographic assumptions".

With such limited information I'm unable to say that the LRRF was calculated correctly. In any event I'm not currently persuaded that Mr I has been treated fairly.

PIC have said that Mr I is currently receiving a pension of £49,905 a year. PIC have also said that if Mr I had decided to start taking his pension in December 2019 then he would now be receiving an annual pension of £50,023.

This means that by continuing to defer taking his pension until October 2021, Mr I is now receiving a lower annual pension than if he had started to receive his pension in December 2019, when he first received late retirement illustrations from PIC. In addition, Mr I has missed out on pension income that he could have received between December 2019 and October 2021. I don't think this is fair or reasonable.

I think that Mr I had been lead to believe through the retirement illustrations that he received from PIC in December 2019 that he would be receiving more annual pension by deferring taking his pension (as would be common), but this has not been the case.

In PIC's final response to Mr I's complaint they said: "As advised in our response sent 24 September 2021, we are unable to provide an explanation as to why the late retirement process is disadvantageous as we do not believe this is the case. If you were to defer your pension you would receive a top up of benefits to account for the years your pension has been deferred."

However, I think that the late retirement process has been disadvantageous to Mr I, as he is now receiving a slightly lower annual pension than would be the case if he had not continued to defer, and he has missed out on annual income whilst he deferred.

I also think that the retirement illustrations that Mr I received in December 2019 did mislead him into thinking that he would receive a much higher annual pension if he continued to defer his retirement age.

I am therefore upholding Mr I's complaint and think that PIC now need to put things right for him.

Putting things right

I think had Mr I understood that by deferring taking his pension after December 2019 he would be receiving a lower annual pension, in addition to having missed pension income whilst he was deferring, then he would not have continued to defer his pension. Instead, I think that Mr I would have taken his pension in December 2019, when he first received late retirement illustrations from PIC.

I therefore think that it's fair and reasonable that PIC now put Mr I back in the position that he would've been had he started to receive his PIC pension in December 2019.

PIC need to calculate how much net pension income Mr I would have received to date of settlement, if he had started to receive his PIC pension in December 2019.

PIC will then need to calculate how much net pension income Mr I has actually received from PIC since he started to receive his pension in October 2021 to date of settlement. The difference is Mr I's past loss and should be paid to Mr I.

In addition, PIC should also pay interest to Mr I on this loss, calculated from December 2019 to the date of settlement at 8% simple. Where interest is being added at 8% simple per annum, this is likely to be subject to tax. If PIC deducts tax, it should tell Mr I how much it has taken off. It should also give Mr I a certificate showing this, if requested by Mr I, so he may reclaim the tax, if appropriate.

PIC have said that the annual pension that Mr I would be receiving now if he had retired in December 2019 is more than the annual pension that he is currently receiving. PIC therefore also need compensate Mr I for this.

PIC should therefore either:

- *Purchase an additional annuity for Mr I, in the same format as the original, sufficient to make up for the difference in future income caused by their error, or:*

- *Pay Mr I a lump sum equal to the purchase price of an annuity (again in the same format as the original) sufficient to make up the difference in future income caused by their error.*

PIC should provide Mr I will full details of their calculations in completing the above. Finally, PIC have offered Mr I £50 in compensation for the confusion caused to Mr I. I believe that a figure of £350 is a more appropriate sum to compensate Mr I for the distress and inconvenience that I believe he has suffered.

My provisional decision

My provisional decision is that I uphold Mr I's complaint against Pension Insurance Corporation plc and Pension Insurance Corporation plc should compensate Mr I as detailed above.

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.

Both Mr I and PIC have responded to my provisional decision. Mr I has said that he's in agreement with the provisional decision. PIC have said that they accept the outcome of my provisional decision.

As both parties have accepted my provisional decision, and no new information or evidence has been presented to me, my decision remains the same.

Putting things right

PIC now need to compensate Mr I as detailed in my provisional decision above.

My final decision

My final decision is that I uphold Mr I’s complaint against Pension Insurance Corporation plc and Pension Insurance Corporation plc should compensate Mr I as detailed in my provisional decision above.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr I to accept or reject my decision before 7 September 2023.

Ian Barton
Ombudsman