

The complaint

Mr S complains that Aviva Life & Pensions UK Limited (Aviva) delayed answering queries about his pension plan whilst the transfer value was falling causing him losses. He would like compensation and an explanation as to why the value fell considering market conditions over the period.

Mr S is represented in his complaint by his financial adviser.

What happened

Mr S's plan with Aviva was taken out in 1985. Linked to the with profits fund, it provided for a guaranteed level of pension on retirement at age 70, or earlier, with a reduced guarantee. His financial adviser, St James Place (SJP), requested information about the plan over a number of years. It was noted that the quoted transfer value had fallen from around £151,000 in 2017 to £131,000 in April 2021. Mr S was considering transferring the plan and with the value continuing to fall he complained to Aviva in June 2021. SJP raised further complaint points on 16 June 2021. SJP said Mr S had intended to retire that month, at age 65. But as Aviva hadn't answered queries, it hadn't been able to advise him properly. SJP said the transfer value had fallen to £125,005 on 16 June 2021, without justification.

Aviva said it had made an error in calculating the values quoted between 2016 and 2019, which were estimates and weren't guaranteed. It said the transfer value was based on the pension being given up, taking current annuity rates and various other factors into account. It apologised and sent Mr S a cheque for £200 for the inconvenience caused. It said the 16 June 2021 value was also an estimate but an accurate transfer value of £124,835.90 had now been calculated. A transfer application was made and £122,439.37 was transferred to SJP on 1 September 2021.

Mr S referred his complaint to our service and our investigator looked into it, but he didn't uphold it.

Our investigator said it was unfortunate errors had been made in the past. But there was no evidence that Mr S had wanted to transfer the plan from Aviva previously. Had he, it would have carried out a correct calculation. He said whilst the basis of transfer value calculations was commercially sensitive, each of the annual statements sent between 2016 and 2019 had quoted the same annual pension of around £8,500 at age 70. Along with a transfer value and a statement that this wasn't guaranteed.

Our investigator said Aviva had written to Mr S in October 2021 after the transfer had been made, referring to a timeline and loss assessment it wanted to undertake. But it appeared this was outstanding, and he'd asked Aviva to look into it. He said as Aviva had clearly stated transfer values weren't guaranteed and had explained why these had reduced, there hadn't been any detriment to Mr S. He said the £200 already paid in compensation was fair, so he wouldn't ask Aviva to do anything further.

Mr S said our investigator had misunderstood the complaint, which wasn't just about the decline in transfer values, but the failure to respond to queries over a period of months

between March and August 2021. Which had prevented him from transferring, resulting in losses as the value continued to fall, by around £8,000.

Our investigator said Aviva had written to SJP several times between December 2020 and April 2021 answering queries about the plan and providing valuations and explanations. The letters stated that transfer values weren't guaranteed and could fall as well as rise. He said Aviva had responded in an adequate manner. Our investigator said as the transfer value required calculation, he thought it had been processed in a reasonable timeframe. He said Aviva's approach was consistent and Mr S hadn't been disadvantaged.

Our investigator said Aviva hadn't explained why it wanted to carry out a loss assessment, but it had asked its third-party administrator to undertake this. Who had written to SJP three times between 9 March 2022 and 9 February 2023 asking for the information it needed for these calculations, but without response. But the information had now been provided and these calculations were in hand.

SJP said the only reason the transfer had taken so long was because of the delays in Aviva responding to queries asking for specific explanations. It said Aviva hadn't explained the valuations or what final bonus had been paid on the plan. Mr S said because of the errors made by Aviva he'd never been in a position to make an informed decision about his plan. He said he and his adviser had regularly discussed the plan at review meetings and had only decided to retain it as the performance seemed to be so good due to the inflated values being quoted from 2017. And he'd missed out on investment opportunities by not transferring sooner.

As Mr S doesn't agree it has come to me to decide.

My provisional decision

I issued my provision decision on 23 August 2023; I explained the reasons why I was planning to uphold the complaint. I said:

I've considered all the available evidence and arguments to decide (provisionally) what's fair and reasonable in the circumstances of this complaint. Having done so, I'm planning to uphold the complaint in part.

There are two main complaints here. I've set out below why I don't think Mr S has been disadvantaged by any initial error in the calculation of transfer values, but why I do think there was some avoidable delay in Aviva processing the transfer, as it accepts. It is now proposing to pay Mr S compensation for this which it says will put him back in the position he should have been in.

The valuations

The transfer value provided by Aviva was based on a conversion calculation to establish the cost of providing the guaranteed pension benefit offered by the plan at the relevant age. The factors considered include prevailing annuity rates.

Depending on the conversion factor used by individual pension providers the transfer value offered on this type of plan can range from good to poor value when compared to prevailing annuity rates. Mr S and SJP have said the reduction in transfer value wasn't reasonable as annuity rates weren't rising (which could be expected to reduce the cash value) during the period. I'll consider this below.

Mr S has also queried Aviva's with profit bonus rates during the period. Some of the historic valuations showed the split between the guaranteed bonuses already added to the plan and final (or terminal) bonus which wasn't guaranteed. As final bonuses weren't guaranteed any adjustments to the transfer value calculated are likely to be reflected in the final bonus shown, as was the case here. It was generally the case that with profit bonus rates were either frozen or reduced through 2020, given the impact the Covid pandemic had on investment markets. Whilst this isn't directly relevant to Mr S's plan, I haven't seen anything that indicates he was singled out in this regard, which would clearly be unfair.

Mr S also says the overstated prior valuations disadvantaged him as they convinced him to keep the plan instead of transferring it. It's unfortunate a mistake was made and not corrected for some time, so I've considered the impact on Mr S of this error.

Whilst Aviva hasn't provided specific details of the error it's clear from the many valuations provided that transfer values weren't guaranteed. If a transfer request had been made, a fully calculated transfer value would have been provided. From mid-2017 annuity rates generally reduced. Ignoring any other factors this could be expected to increase the transfer value. From February 2021 annuity rates generally rose, which would be expected to reduce the transfer value. So, there was always the risk that the transfer values quoted, could fall. There is some evidence that the transfer process was started in July 2018 by SJP. As Aviva wrote to it asking for confirmation that Mr S was being provided with regulated financial advice. It isn't clear why the transfer didn't proceed then.

SJP has provided some emails following reviews with Mr S in July 2018 which say:

"For now it is difficult to compare scheme benefits on a like for like basis due to the guaranteed annuity rates contained at retirement age and so I will recommend that you leave the funds invested with AVIVA for now.

Once (Mr S) decides to retire I will be able to compile a direct comparison of benefits and then make a recommendation as to whether it is in your best interests to consolidate your various retirement funds."

I haven't seen any evidence of how any appraisal was carried out when it was concluded the investment was doing well and should be retained with Aviva as Mr S has said. But a "high" transfer value relative to prevailing annuity rates would generally indicate transfer was beneficial.

By 2021, Aviva had corrected the error in its calculations and Mr S's transfer was completed on 1 September 2021, shortly after his 65th birthday, with £122,439.37 transferred to SJP. By then the guaranteed pension from the plan would likely to higher than the £5,912.93 previously advised by Aviva at age 65, but only marginally so. And in September 2021 a comparable annuity rate was around 5.1% for a 65 year old, implying a cost of buying that guaranteed pension of around £116,000. This is less than the transfer value Aviva paid, suggesting it wasn't unreasonable given the terms and conditions of the plan.

Had a transfer been requested earlier, Aviva might have advised the actual transfer value was somewhat lower than had been indicated. Possibly too low to make the transfer appear "good" value. In which case Mr S presumably wouldn't have proceeded with the transfer anyway. Consequently, I don't think the valuation information provided to Mr S from 2017 misled him about the benefit or otherwise of retaining the plan or transferring it.

Delays

I've considered whether Aviva delayed the transfer by failing to respond to queries in a timely fashion. I can see that SJP made many enquiries over a period of several years, often requesting the same information as previously provided along with updated transfer values. This pattern seemed to repeat itself in the months before the actual transfer.

SJP raised queries about the plan and Aviva confirmed details on 2 December 2020. SJP requested a quotation of benefits if Mr S was to retire at age 65 (June 2021) on 3 March 2021. The next day SJP asked for a breakdown of funds and for an explanation about under performance, details about charges and information on the guaranteed pension. Aviva issued the requested retirement quotations and various application paperwork for the different options on 7 March 2021. It then sent SJP a copy of the policy conditions, details of funds and charges and of the guaranteed pension applying on 16 March 2021, explaining, as it had previously, that the plan was a deferred annuity contract.

On 18 March 2021 Aviva confirmed projections couldn't be provided within six months of retirement. SJP then chased up the information requested, and Aviva emailed the letter of 16 March 2021 and provided further information about performance, the plan and conditions applying on the 8 and 9 April 2021. It provided the estimated retirement fund at age 65 on 23 April 2021. SJP asked more questions on 10 May 2021, including the start date of the plan and whether the guaranteed pension included tax free cash. Presumably it didn't have the information it felt it required to advise Mr S about transferring before then.

Aviva sent further information on 16 June 2021, by which time Mr S had already complained about the reducing transfer values. SJP then complained about delays in responding to its queries. Aviva wrote on 16 July 2021 confirming again that the plan had no fund value and provided for a pension to be paid. And that the transfer value would be based on the pension value "based on annuity rates in force at the time. And that;

"It was up to the policy holder and his or her adviser to decide whether it is better to take the transfer value or to retain the benefit under the policy."

It continued that annuity rates were kept under constant review and that:

"Annuity rates are presently cheaper than they were a few weeks ago and this means that the current transfer value is lower than previously quoted."

SJP then requested a transfer on 27 July 2021 but sent incorrect application forms. Aviva sent the correct forms to SJP on 30 July 2021. These were returned on 12 August 2021 and Aviva contacted Mr S to request proof of his national insurance number which he provided on 24 August 2021 and the transfer was completed on 31 August 2021.

I've looked at the information Aviva sent in response to the queries raised by SJP during 2021. Much of this had been provided earlier and I think the further explanations given were clear. SJP was querying the basis of the valuation provided and raising queries about investment performance and bonuses, which weren't directly relevant to the transfer figure provided. And the queries raised weren't something I'd expect Aviva to be able to immediately respond to. And as noted above the transfer value doesn't appear to be obviously unfair given the benefits it was based on.

However, Aviva accepts there were delays that resulted in both a fall in the transfer value and a delay in the re-investment with SJP being made. I asked Aviva about this. It said there were two occasions when it hadn't met its internal ten working day target to respond to queries raised by SJP. But for these delays it says the valuation date should have been 21 July 2021 rather than 13 August 2021. With it making payment to SJP on 2 August 2021 rather than 31 August 2021.

Aviva says the value on 21 July 2021 was £125,005.48 rather than the £122,439.37 actually transferred, a difference of £2,566.11. It says the delay in re-investment with SJP caused a further loss. With the total loss being £4,650.92, based on the details provided by SJP. Aviva has proposed to make payment directly to Mr S subject to a notional tax deduction of 15%, so the net payment would be £3,953.32. This assumes he is a basic rate taxpayer. Our service hasn't checked these calculations, but I've asked that Mr S is provided with a copy of them for his consideration.

So, Aviva did cause some delay and in general terms I think it's offer here is fair. But I think interest should be added to the compensation calculated as Mr S has been denied the use of the funds for many months. Not all of that delay was Aviva's responsibility, so I've set out how I think things should be put right below.

Putting things right

My aim in awarding compensation is to put Mr S back into the position he would have been in as closely as possible but for the errors made.

- Aviva should calculate the actual transfer value on 21 July 2021 and any loss caused by the delayed re-investment of the transfer. Aviva says based on when SJP invested the funds sent this would have been 6 August 2021. If Mr S or SJP dispute this is a reasonable date they should provide appropriate evidence.*
- Aviva has already undertaken the calculations outlined which indicate a total loss of £4,650.92. It proposes to pay Mr S £3,953.32 after a notional allowance for tax.*
- When benefits are paid from a pension plan they provide a taxable income. So, adjusting the compensation to notionally allow for any income tax that would otherwise have been paid ensures the compensation is a fair amount. It isn't a payment of tax to HMRC, so Mr S won't be able to reclaim any of the reduction after compensation is paid.*
- The notional allowance should be calculated using Mr S's actual or expected marginal rate of tax at his retirement age. If Mr S is a basic rate taxpayer, the reduction would equal 20%. However, as he would have been able to take a tax-free lump sum, the reduction should be applied to 75% of the compensation, resulting in an overall reduction of 15% as proposed by Aviva.*
- If Mr S isn't a basic rate taxpayer, he will need to confirm this so the assumption can be adjusted so he receives appropriate compensation. It won't be possible for us to amend this assumption once any final decision has been issued on the complaint.*
- I also think it's fair that interest should be added to the compensation due. Aviva first requested information from SJP to complete its calculations on 9 March 2022, so around six months after it should have paid the correct transfer value to SJP. The information Aviva needed was sent on 17 May 2023, but it didn't complete its calculations until 7 July 2023, so around another three months delay to give around nine months in total.*
- So, the delays in addressing the issue of compensation that are Aviva's responsibility run from 2 August 2021 to 9 March 2022, then from 17 May 2023 until the date of settlement. Aviva should add interest to the notional compensation amount at 8% per year simple from these dates.*

- *Income tax may be payable on any interest paid. If Aviva deducts income tax from the interest, it should tell Mr S how much has been taken off. Aviva should give Mr S a tax deduction certificate in respect of interest if Mr S asks for one, so he can reclaim the tax on interest from HMRC if appropriate.*
- *Aviva should provide Mr S with a simple calculation of how it arrived at its figures.*
- *I think Mr S has been inconvenienced by what has happened but that the £200 gesture of goodwill payment already made is fair in the circumstances.*

I asked both parties to come back to me with any further evidence or points they wanted me to consider.

Response to provisional decision

Mr S said he accepted my decision. But said that he wasn't a taxpayer in the current tax year and asked whether the 15% notional deduction to the compensation could be reclaimed.

Aviva disagreed with my decision. It said adding interest to the compensation wasn't fair as its calculations already considered the whole period up until 23 July 2023.

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 decided to uphold the complaint in part.

Aviva did cause a delay, so it's fair that Mr S be put back into the position he should have been in. I've reconsidered Aviva's calculations and I agree that as they are up to date, they do fairly provide redress for the delays it caused and put Mr S back into the position he should have been. So, it isn't necessary for them to add interest to the calculated redress, unless there is an unreasonable delay in making payment to him.

In terms of the notional allowance for tax I referred to, this is to avoid Mr S being paid too much compensation. As the allowance is notional there isn't anything he can claim back from HMRC. Notional deductions follow a long-established legal precedent dating back to 1956 with a Court case that was decided by the Law Lords. Called the Gourley Principle, in simple terms, it means that tax should be taken into account when determining fair compensation.

So, what I'm considering here is Mr S's likely marginal rate of tax when he's fully retired (he's now 67) and drawing out the pension as income. His income will include State Pension which is taxable. I asked Mr S about his current income, and he confirmed he receives the State Pension, and this is currently just under the personal tax allowance. So, only a relatively small amount of income could be drawn from his pension before he would be subject to income tax.

Mr S might be able to manage his finances and use capital or tax free income sources such as ISAs, but I think it's reasonable to conclude he would most likely be subject to basic rate tax on the income from his pension, when he does draw this. Therefore, I think it is fair that a 15% notional deduction for tax be allowed for, which takes account that 25% of Mr S's pension could be paid as a tax-free cash sum.

The alternative would be for Aviva to make the payment directly to Mr S SJP plan, where no deduction would be made. This assumes that level of contribution could be paid under tax rules, which may not be possible. But assuming it was possible the amount he would receive as compensation would be the same if he then took his pension benefits and paid income tax on them. So, it is fair compensation and does put him back into the position he should have been in.

Putting things right

Aviva has already undertaken the calculations outlined which indicate a total loss of £4,650.92. It proposes to pay Mr S £3,953.32 after a notional allowance for tax.

When benefits are paid from a pension plan, they provide a taxable income. So, adjusting the compensation to notionally allow for any income tax that would otherwise have been paid ensures the compensation is a fair amount. It isn't a payment of tax to HMRC, so Mr S won't be able to reclaim any of the reduction after compensation is paid.

Mr S is likely to be a basic rate taxpayer when he takes the benefits, so the reduction would equal 20%. However, as he would have been able to take a tax-free lump sum, the reduction should be applied to 75% of the compensation, resulting in an overall reduction of 15%, as proposed by Aviva.

I think the £200 Aviva has already paid Mr S is fair compensation for the inconvenience he has suffered.

My final decision

For the reasons I've given above and in my provisional decision, my final decision is that I uphold this complaint against Aviva Life & Pensions UK Limited.

I direct Aviva Life & Pensions UK Limited to pay the compensation it has already calculated to Mr S which I consider to be fair in the circumstances of the complaint.

Aviva Life & Pensions UK Limited must pay the compensation within 28 days of the date on which we tell it Mr S accepts my final decision. If it pays later than this, it must also pay interest on the compensation from the date of my final decision to the date of payment at 8% a year simple.

If Aviva Life & Pensions UK Limited considers that it's required by HM Revenue & Customs to deduct income tax from that interest, it should tell Mr S how much it's taken off. It should also give a certificate showing this if Mr S asks for one, so he can reclaim the tax from HM Revenue & Customs if appropriate.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 13 November 2023.

Nigel Bracken
Ombudsman