

The complaint

Mr M is unhappy with Phoenix Life Ltd, believing they've deducted too much tax on a pension shortfall payment made to him, following their earlier mistake in transferring an incorrect sum to a new pension provider.

What happened

Mr M had a pension policy with Phoenix. In 2019, he approached them and asked them to transfer this pension to a new pension provider who I'll call 'SL' here. On 19 September 2019 – the date of the transfer – his pension was worth £162,729.68, but Phoenix mistakenly transferred only £154,717.16 (a shortfall of £8,012.52).

This came to light in October 2022, following an internal Phoenix review. Phoenix immediately offered to make a cash payment to Mr M for the shortfall. After tax had been deducted, £6,925.25 was paid to Mr M by cheque in October 2022. Unhappy with this, Mr M complained to Phoenix, raising the following complaint points:

- He was unhappy with the mistake, and the length of time it took to come to light.
- Phoenix sent him a cheque for the underpayment, rather than pay that sum to his new SL policy.
- Mr M was also unhappy that tax was deducted from the underpayment cheque.
- And Mr M thought he'd lost out on investment growth, in relation to the underpayment, during the period in question.

Phoenix responded. They apologised for not checking first with Mr M to find out whether he'd have preferred the funds to be paid to his new SL policy. But having paid the sum to Mr M, they were required to deduct Income Tax from the amount paid.

Phoenix also contacted SL in March 2023, to find out how much Mr M's pension would now be worth had the correct amount been transferred in 2019. SL responded on 30 May 2023, confirming that had the 'extra' amount of £8,012.52 been invested with them at the same time as the main transfer, the extra investment units it would have been able to purchase at that time would now cost £9,398.93 to purchase.

Phoenix therefore offered to pay Mr M a further amount of 'loss' compensation of £2,473.68 (the difference between £9,398.93 and the net payment previously paid of £6,925.25). They also offered to pay Mr M £200 compensation for the trouble and upset caused, a further £200 for their delay in responding to the complaint, and £40 towards the cost of phone calls he'd made.

Unhappy with this offer, Mr M brought his complaint to us in July 2023. Phoenix then told us that they'd be willing to undertake a fresh loss calculation and pay the full loss calculation to Mr M's SL policy – assuming they'd be willing/able to receive such sum, if Mr M would be willing to return the £6,925.25 previously paid to him. They also offered a further £100 compensation for the further inconvenience caused.

However, Mr M confirmed he wasn't now able to return all of the £6,925.25 payment. Furthermore, he didn't believe Phoenix's updated loss calculation offer properly took account of the tax that had been deducted.

One of our Investigators considered Mr M's complaint, but was satisfied Phoenix's offer of compensation was fair, including their offer to pay the full loss/shortfall to Mr M's SL policy – if Mr M was able to return the funds he'd already received.

Mr M was unhappy with our Investigator's conclusions, still believing tax had been deducted from the 'shortfall' payment, which it shouldn't have been. And despite further exchanges with our Investigator on this matter, no agreement could be reached, and Mr M asked that his complaint be considered afresh by an Ombudsman – and so it's been passed to me to consider Mr M's complaint and issue a Decision accordingly.

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.

It's not in dispute here Phoenix made a mistake by not transferring the full value of Mr M's policy to SL when they should have done. The question for me to consider is whether Phoenix have done enough to compensate Mr M for their mistake, and if not, tell them what I think they should do.

It's important to begin by making clear that, where a business has made a mistake, we'd expect that business to take all necessary steps to put their customer back into the position they would have been in had the mistake not occurred.

Ordinarily, in a case such as this, I'd be asking Phoenix to contact SL to find out how much Mr M's policy would now be worth if the full (correct) amount had been transferred in 2019. If the policy would now be worth more than what the current (lower transfer) policy is worth, I'd be telling Phoenix to pay the difference to SL so that it could be added to Mr M's SL policy – returning it to the value it would have been had the mistake not occurred. There would be no tax deduction made because benefits from the SL policy hadn't been taken yet.

I acknowledge that Phoenix have now apologised to Mr M that they didn't do this at the outset – which I think they should have done (or at least made enquiries with Mr M to see if this was how he wished to resolve their mistake). I think it's fair to conclude that had they done that, it's highly likely Mr M would have agreed to having the necessary funds credited to his SL policy as I've described above and avoided considerable distress and inconvenience (D&I) caused by the mistake. I'll return to the issue of compensation for the D&I Mr M has experienced later in this Decision.

I also acknowledge that Phoenix have offered to undertake an updated calculation, if Mr M was able to return the funds they *did* pay him (£6,925.25). This is a fair offer, and again something I'd have asked Phoenix to do as a means to place Mr M back into the position he would have been in had the mistake not occurred.

However, Mr M has told us that he is no longer able to return the funds, because he has utilised some of them – so that is no longer an option here. I'm aware too Mr M has been able to reclaim an amount of the tax that was deducted from HMRC – approximately £510.

The above being the case, I need to return to the calculations that have taken place regarding the lump sum payment. First and foremost, in situations where a business has to

pay a pension 'loss/shortfall' lump-sum figure to a consumer in circumstances such as these, that business would be expected to deduct tax from that payment. I'll briefly explain why.

The 'shortfall' figure *should* have been paid into Mr M's SL pension. If it had been, there'd be no tax deducted from that figure – it would simply sit with his originally transferred pension, increasing (or decreasing) in value as the value of his investments changed. However, as soon as Mr M started to draw this pension, those drawings would be subject to tax. Mr M would be able to take 25% of his pension as a tax-free amount, and he'd pay income tax on the remaining drawings. So, in simple terms, Mr M would be charged income tax on any drawings made – which would include the 'loss/shortfall' transferred in – at his marginal rate of tax at that time, when he chose to take his benefits.

Because this is what *would* have happened to the 'shortfall transferred' amount, it means the same calculations must be applied to the one-off shortfall payment that Mr M received from Phoenix. It must be treated, as much as possible, in the same way. Tax would have been deducted from it if it was drawn from his pension, so tax must be deducted from the one-off payment that was made directly to him. Were this not to happen, it would have the effect of putting Mr M in a *better* position than he would have been in had the mistake not occurred – he'd have benefitted from receiving the transfer shortfall without any tax being deducted.

So, I think Phoenix were correct in principle to deduct the tax from the payment they made to Mr M in October 2022.

However, I don't think Phoenix undertook the initial shortfall calculation correctly. They sent Mr M the shortfall amount three years after their mistake, but didn't add interest for late payment, and/or seek to identify the updated value of that shortfall amount. But that has now changed. As I said, Phoenix approached SL, who provided calculations to show that, had the full (correct) amount have been transferred in 2019, the £8,012.52 shortfall would have been used to purchase investment units that would cost £9,398.93 to replace as at 30 May 2023. So, this is the maximum amount Phoenix would have *needed to pay* to SL to return Mr M (his SL policy) to the position he would have been in had their mistake not occurred. Accordingly, I think it's fair this is the figure which Phoenix must base their lump-sum redress to Mr M on.

Phoenix have already paid Mr M the tax-reduced sum of £6,925.25. They've offered to pay him a further amount of £2,473.68 as compensation, taking the full amount of compensation offered to £9,398.93 – in other words an amount equivalent to the total loss in value his new SL pension had experienced as a result of Phoenix not transferring the correct amount in 2019.

What's more, the net effect of this offer is that Mr M would have benefitted by receiving the full transfer shortfall without deduction of any tax – essentially placing him in a better position than he would otherwise have been in (a) had the shortfall been transferred to SL when it should have been, and (b) by him receiving an adjusted shortfall figure without tax being deducted. Phoenix have said, because of their mistakes, they are prepared to pay this extra amount to acknowledge and apologise for the mistakes they've made.

Given what I've explained above, I think Phoenix's offer is a fair one, and I won't be asking them to do anything to increase that offer.

Distress and Inconvenience

As I said above, notwithstanding Phoenix's fair offer to compensate Mr M for the shortfall, I think it's clear Mr M experienced distress and inconvenience that could have been avoided. And it's only fair that Phoenix pays a separate sum to Mr M as compensation for the distress their actions/mistakes have caused him.

Phoenix have already offered to pay Mr M a combined £300 compensation for the distress caused by their mistakes, £200 for the delay in addressing his complaint, and £40 to cover the cost of the phone calls he's made.

Firstly, I must make clear that whilst this Service is able to consider many complaints about financial services, as set out in the Financial Conduct Authority's 'DISP Rules', there are certain things we can't consider. One of those is 'complaint handling'. What that means is that ordinarily I can't specifically tell a business to pay any consumer an amount of compensation in relation to the way a business has handled that person's complaint.

Here, however, whilst Phoenix have said that £200 compensation is specifically for "*the delay in responding to [Mr M's] complaint*", I think it's clear that delay was partly caused by the actions Phoenix took in engaging with SL to try and understand the full extent of Mr M's potential loss. In other words, it related to the merits of Mr M's actual complaint. Accordingly, I'm satisfied that I'm able to comment on that element of Phoenix's offer here.

So, the question for me is whether £500 (plus £40 costs) represents a fair award for the distress Mr M experienced. The amounts this Service awards for D&I are fairly modest in value. Our D&I awards are not designed to punish a business, but rather to put a monetary value on the distress a business' actions have caused. Guidelines setting out our approach to such awards can be found on our website.

So, taking account of what I've said above, and having careful regard to our guidelines on this subject, I think a D&I award of £500 is appropriate here – and so I won't be asking Phoenix to increase the total offer they've already made to Mr M in this regard.

Putting things right

Phoenix has already made an offer to put things right, which I think is fair in all the circumstances. So, Phoenix should put things right for Mr M in the way they've already offered which, for the avoidance of doubt, requires them to do the following:

- Pay Mr M, if not already done, £2,473.68 as compensation for the transfer shortfall.
- Pay Mr M, if not already done, £500 compensation for distress and inconvenience, plus a further £40 to cover phone costs incurred.

The above payments should be made within 28 days of being informed of Mr M's acceptance of this decision.

My final decision

Phoenix Life Ltd has already made an offer to put things right, and I think that offer is fair in all the circumstances. So, I require Phoenix Life Ltd to put things right for Mr M in the way they've already offered, as detailed above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 15 March 2024.

Mark Evans
Ombudsman