

The complaint

Mr S complains that Aviva Life & Pensions UK Limited (Aviva) deducted tax from his pension drawdown plan using an incorrect personal allowance. He says HMRC has provided a solution to the problem, but Aviva hasn't acted upon it, causing him to have to use his savings to meet his everyday expenditure. He would like to be compensated for his various losses.

What happened

Mr S has held a drawdown plan with Aviva since February 2018. He was onboarded onto Aviva's platform and started to make regular income withdrawals which Aviva set with an initial "end date" of 21 April 2022. At the start of the 2023/2024 tax year he asked Aviva to pay him a monthly income of £4,000 – which was broadly in line with his requests from the previous few years. Mr S says his personal tax code at that time was 1383M. But he says that when he began receiving the payments his payslips showed income tax deductions of £800 using the basic rate (BR) tax code. He says that when he checked his HMRC "*my gateway*" facility it did show the correct tax code although it stated that the end date was 21 April 2022.

So Mr S complained to Aviva that he'd paid additional tax and was now "out of pocket." After further discussions Aviva concluded it hadn't done anything wrong, and that Mr S needed to contact HMRC to resolve the issue. But Mr S says HMRC told him that Aviva had issued it with a P45 document which effectively "terminated" the arrangement in 2022. HMRC said Aviva needed to provide it with various documentation to be able to correct Mr S' position and refund any overpaid tax.

In the meantime Mr S says that as he had a shortfall in his expected annual income, he had to withdraw funds from his ISA investment in September and October 2023 to meet the shortfall.

Mr S complained to Aviva again but didn't receive a response within the standard time usually given to answer complaints – so he brought his complaint to us.

Aviva then provided a final response in which it said that it hadn't provided HMRC with a P45 and had simply used the tax code it was sent by HMRC. This was by way of notification of a BR code in June 2022 and a new individual tax code in February 2024. So it thought it had acted correctly and referred Mr S back to HMRC. It said Mr S transferred his plan to a new provider before it received the new tax code.

One of our investigators looked into the matter and thought Mr S' complaint should be upheld. She made the following points in support of her assessment:

- On balance she thought Aviva did inform HMRC that Mr S was a "leaver", and this was the cause of the generation of a new BR tax code for him.

- Mr S had now received a refund of the overpaid tax but should be paid interest at 8% simple pa for each income amount he'd requested when it should have been paid to him.
- But she didn't think Mr S should be compensated for the loss of the tax free status of the funds he withdrew from his ISA to cover the income shortfall, as he had unused ISA allowance from that year and could have repaid the tax refund into his ISA.
- She also didn't think Mr S should be able to replace the units that had been cancelled from his pension at the same unit price with the refund he'd received, because she thought the number of units sold to provide the gross income was correct and it was the additional tax that was deducted that was the issue.

Mr S said he wasn't seeking compensation for any loss to the unit price of his pension funds but did intend to replace the ISA funds he'd had to withdraw. And he calculated that as the unit price had now risen – and he would end up paying two lots of dealing costs – he would suffer a loss of around £150, for which he would like to be compensated.

The investigator said she had considered this point but thought the ISA sales were quite in excess of the refund that was due and noted Mr S hadn't made any withdrawals during the previous tax year when his position seemed to be the same.

Mr S confirmed that his complaint related to events in the 2023/2024 tax year and that he was only claiming compensation for any loss in purchasing new ISA units – which he was no longer able to do through an ISA because he'd used his full allowance – up to the value of the refund, not the full amount of withdrawal he'd made.

Aviva also disagreed with the assessment. It said that although it understood the investigator had reached their conclusion on “the balance of probabilities” it had previously confirmed that it hadn't made an error with Mr S' policy and that it had implemented the correct tax code. It didn't think it was fair to hold it responsible for any financial loss without firm proof from HMRC that it had sent an erroneous P45.

Mr S confirmed that around April 2024 HMRC refunded him the tax that he had overpaid.

My provisional decision

As no resolution could be found the matter was passed to me to review and I issued a decision in which I provisionally upheld Mr S' complaint. I made the following points in support of my decision:

- It was pleasing to hear Mr S had now received his tax refund from HMRC and therefore was no longer incurring a direct financial loss as a result of the incorrect application of the tax code.
- So I now needed to consider Mr S' claim that he'd suffered a loss from having to make withdrawals from his ISA investment to cover the shortfall in his pension income, and also whether a compensatory payment for the impact the matter on Mr S was warranted.
- It hadn't been possible to obtain the information from HMRC to conclusively prove whether Aviva had sent it a P45 document in June 2022 – so I had to decide what I thought had happened on the “balance of probabilities”.
- But it was clear that Aviva had suffered a “systems issue” in and around March 2022 which led to it incorrectly reporting some policyholders to HMRC as “leavers” though the issuing of P45's.
- Although Aviva says its records demonstrate that Mr S wasn't among those affected and it didn't issue a P45 for him, HMRC told Mr S in a telephone call in April 2022

that it had received a P45 from Aviva which led to it sending Aviva a change of tax code at that time. The timing of all these events seemed to support Mr S' claim and, on balance, I felt that this was more likely than not to explain the reason behind the change of tax code.

- I thought there was an absence of any other reasonable explanation for what happened as I thought it unlikely that HMRC would adjust an individual's tax code without some request or reason to do so, and there was no evidence to support the idea that Mr S had any communication or interaction with HMRC at this point. So the more likely explanation was that Aviva did issue a P45 to HMRC.
- Although Mr S had now received a refund of the overpayment of tax, he had been deprived of the correct level of income from April 2023 to the time he received the refund. So I said Aviva should pay interest at 8% simple pa on those funds. But I didn't think it was fair for Aviva to compensate Mr S for any investment loss from the funds not remaining in his pension plan during that time as this would effectively compensate him twice for the same deprivation.
- I considered Mr S' claim for the investment loss – and other costs – that he said he suffered from encashing part of his ISA to make up the pension income shortfall. Based on the evidence I'd been provided with I was satisfied Mr S had used his ISA to withdraw funds to support the income shortfall he'd suffered. I thought Aviva should work out any loss of the growth of the units he encashed – up to the amount of additional tax he was charged – and add 8% interest from that point to the date of any final decision.
- I also considered that for any additional withdrawal from the ISA Mr S would ordinarily have taken this money from his pension plan. Both products have some degree of tax efficiency so I thought Aviva should compare the growth on the units withdrawn from the ISA with the growth on the units for the same value in the pension plan. If the ISA units would have performed better, that would have been an additional loss to Mr S and should be paid into his pension plan as redress.
- I thought the £250 compensation set out by the investigator in his assessment for the impact this matter had on Mr S was fair and reasonable in this case – and that Aviva should pay that sum to Mr S.

Responses to my provisional decision

Mr S generally accepted the outcome but wanted to confirm that he held Fixed Protection 2015 on his pension plan. So he was anxious for any redress not to be paid into the plan in case it was viewed as a pension contribution which might lead to a significant tax charge if viewed as a breach to his transitional protection of the lifetime allowance.

Aviva didn't agree with my provisional decision. It said:

- It was sorry that Mr S had been made aware of its systems issue in 2022 – which was an internal error – as it had investigated this matter and found that Mr S hadn't been affected. But it also thought its position was supported by HMRC who had said it received the P45 on 21 April 2022, which was around one month after the problem arose.
- It provided copies of P60's it had issued to HMRC in May 2022 and 2023 for Mr S. It noted that HMRC didn't change the tax code back on receipt of these communications.
The first of these was issued less than one month before HMRC had said it received the P45 and several months before it received confirmation of the BR tax code on 27 June 2022.
- It also contacted HMRC about Mr S' tax code to clarify if any errors had been made and received an email which confirmed Mr S had been and still was on the correct

tax code. It said HMRC ought to have raised the possibility of an error at this point and this was evidence which confirmed to Aviva that it hadn't made any errors.

- It hasn't to date received any evidence from HMRC that it did provide the erroneous P45 document, and because it's not possible to demonstrate that it didn't send the P45 it thought the onus was on HMRC to prove otherwise.
- It thought that as Mr S had now received his refund for the overpaid tax this was further proof that the tax code HMRC issued was wrong and contradicted the email it previously sent to Aviva.
- It thought that, on balance, the issue was more likely to have been caused by HMRC and that this complaint shouldn't be upheld on "the balance of probability" for that reason.

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.

And having carefully considered the further submissions I've received following my provisional decision I see no reason to depart from my provisional findings.

I should first say that I can understand if there has been some frustration from both parties in the time taken to issue this final decision. That was because I needed to make every endeavour to get information that would ensure I had reached the right and most appropriate outcome here. I hope this final decision will now give all parties the necessary closure required.

As I said in my provisional decision, during the course of our investigation Mr S did eventually receive a refund for the overpaid tax. So my only consideration around that matter is the interest that should be added to the payment for the deprivation of the funds and whether Mr S has been impacted by what happened to him. I'll address those points later in the decision.

This decision focuses on the remaining complaint points Mr S made around any financial losses he suffered as a result of having to make adjustments across other areas of his finances to make up the shortfall in the income he expected to receive. In order to look at that I've first considered who I think might be responsible for the production of an incorrect tax code.

The responsibility for the incorrect tax code

Mr S says he had been receiving income from his Aviva pension plan without difficulty until the start of the 2023/2024 tax year, when instead of his tax code of 1383 being used, his income was taxed at basic rate. There's no dispute that this was caused by a new tax code being issued to Aviva by HMRC in June 2022, which led to that new tax code being applied for the following tax year. But the question here isn't the application of the tax code but to consider why it was issued and who was most likely to have been responsible.

I've been provided with evidence to confirm that Aviva had an issue with its systems in March 2022 which led to it reporting some policyholders as being "leavers" or in other words that their income withdrawal arrangements had come to an end.

In that situation I can understand why Aviva then issued P45's to HMRC for those policyholders in error. If this had affected Mr S and Aviva had identified him as being one of those policyholders then there's little doubt it would have accepted responsibility and taken the necessary steps to put things right.

But Aviva says that Mr S didn't appear on that list and there's no evidence to suggest it did send an erroneous P45 to HMRC in error. It says it can't provide evidence that it didn't send something that it has no record of sending, but it simply implemented a new tax code sent to it by HMRC as it was required to do.

Mr S says however that HMRC told him that it had received a P45 from Aviva on 21 April 2022 – just a few weeks after it suffered the systems malfunction. He says there's no other plausible explanation for why a P45 was then subsequently issued.

Of course to definitively prove what happened in April 2022 would require further evidence from HMRC, but unfortunately over a period of many months it's simply not been possible for any of the parties involved here to obtain that evidence. So, and to ensure that both parties receive an outcome to this matter, I've made my decision here on the balance of probabilities.

Looking at the possible alternatives there's no evidence to suggest that Mr S did anything to provoke HMRC to issue a new tax code for him. And I have no reason to think that HMRC would have issued a new tax code for Mr S unilaterally without a request from another party that it needed to make a change. Aviva has said that HMRC might simply have made an error and the balance of probability points to that fact, but I think the facts that are known here point to the probability being that Aviva's systems malfunction was more likely to have caused these actions.

Firstly the timing of Aviva's system error in March 2022 would show a reasonable likelihood that any P45's sent out in error would have been received by HMRC at some point in April 2022 – which is when HMRC confirmed it received the erroneous P45. HMRC then issued the new BR tax code in June 2022 which doesn't seem an unreasonable timescale in which to have updated its systems and issued the new code. So this sequence of events, close to the time of the systems malfunction, would seem the more likely to have happened. I know Aviva says Mr S doesn't appear on its record of affected policyholders and it has no evidence within those records of issuing a P45, but in the same way Aviva thinks HMRC might simply have made a mistake, it's also possible that Aviva's records were incomplete, especially as the issue was caused by a failure of its systems.

Aviva has also said that it sent HMRC P60's for Mr S in 2022 and 2023 following which HMRC didn't raise any issues about Mr S' tax code. It also had later communication with HMRC in which it "confirmed" Aviva hadn't made any errors with the tax codes. I'm not persuaded that the P60's would have caused HMRC to launch an investigation to compare what was on them against the tax code it had sent. There would be little reason for it to do that.

And, looking at the email trail between Aviva and HMRC, this was after the error had been identified and all parties were trying to find a resolution. I haven't seen any evidence to support the claim that HMRC confirmed Aviva hadn't made any errors as it said, *"as I stated below, in this case the individual's new tax code was issued 8 February 2024. Therefore, it should be used from that date for payments made. Payments issued prior to 8 February should be taxed on the previous tax code."* This was just a statement of the facts of the matter and doesn't, in my view, support the claim that HMRC told Aviva it hadn't done anything wrong – which was the basis on which Aviva decided it hadn't made an error.

So, taking all the contemporaneous evidence available to me into consideration, I think, on balance, that it was the erroneous P45 being issued for Mr S to HMRC which was the more likely reason for this situation occurring.

The claims for loss of investment growth and tax benefits from both Mr S' ISA and pension fund

Mr S has now received his tax refund so there's no outstanding financial loss there. But he should have received that extra money each time he was due to receive an income payment after April 2023.

So I think Aviva should pay Mr S interest for being deprived of those funds at 8% simple per annum from April 2023 to the time he received his refund. Income tax may be payable on any interest paid. If Aviva deducts income tax from the interest, it should tell Mr S how much it has taken off. Aviva should give Mr S a tax deduction certificate in respect of interest if he asks for one, so he can reclaim the tax on interest from HMRC if appropriate.

Turning to any loss of investment growth Mr S may have suffered from his pension fund, I think the gross amount of income that he was paid was correct, so I don't think there has been any loss of investment growth. But in any case I've said that Aviva should pay Mr S interest for being deprived of his money so any consideration of investment loss growth from the pension would likely him compensate him twice for the same error – which I don't think is fair in this case.

Mr S' primary complaint regarding investment losses arises from his ISA, from which he says he had to partially disinvest funds in two separate tranches to replace the income he expected from his pension to meet his bills and financial commitments during this time. He says he can't now replace the money in his ISA because he has no annual allowance remaining and the cost of buying back the lost ISA units has also increased.

I would need to see strong evidence of a correlation between Mr S' actions with his ISA and the need to replace his "lost" income because, deciding that a loss from alternative investment funds arising from an error such as this should be upheld, is more difficult to demonstrate.

Mr S has shown us that he sold units in his ISA in September and October 2023. This was several months after the incorrect tax code was applied and Mr S began to receive less income. But I note that Mr S' first action was to try to resolve the problem with Aviva and then subsequently with HMRC. And it would seem that HMRC did provide a course of action that might have corrected this situation. But by August 2023 Mr S received a response from Aviva which confirmed the matter couldn't be resolved at that time.

So I don't think it was unreasonable for Mr S to consider he might need to take an alternative course of action to "plug" his income shortfall and this is supported by his actions in withdrawing funds from his ISA the very next month. I've seen evidence that the first withdrawal was broadly in line with amount of income he had "lost" from his pension withdrawals, so I'm satisfied it was for this purpose. The second withdrawal though was for significantly more than the "missing" income. I've considered that point carefully as I said previously I would expect to see a strong correlation between Mr S' position and his actions. I asked Mr S to explain the reason for this and he confirmed that he needed to pay for an imminent holiday, but that he was only requesting the balance of the withdrawal that matched to his lost pension income.

I'm persuaded this demonstrated that firstly Mr S didn't have available funds elsewhere to pay for his holiday and also the careful budgeting of his everyday expenses and commitments against the pension income he used to pay for those things. I think it's likely that, but for the error with the tax code, Mr S would ordinarily have withdrawn the additional

funds from his drawdown plan. But in this instance, I don't think it's unreasonable that Mr S wouldn't have withdrawn more money that he needed from his drawdown plan with the potential investment loss and additional tax implications this would have caused.

So I don't think it's unreasonable for him to have taken the actions he did in accessing those funds from his ISA investment. I don't think the withdrawals were excessive in consideration of the income he'd lost, and the timing of those withdrawals is also consistent with putting the shortfall right – especially when taking into account the time he spent to resolve the issue with Aviva and HMRC. I'm also persuaded that Mr S would have repaid the proceeds of the tax refund back into his ISA if he'd received it in a timely manner.

But as it took over a (tax) year from the identification of the error until he received the refund, by which time he had maximised his ISA allowance, he was unable to repay funds back into it. So I'm satisfied that Mr S did access his ISA funds for good reason and that this was because of Aviva's error with regards to his tax code. I'll set out below what Aviva should do to put this right.

Putting things right

So for the amount which Mr S would ordinarily have had, i.e. the amount of additional tax which was charged and to which he was denied access, I think Aviva should calculate the (gross) loss of growth on those units for the amount which was withdrawn up to the date the refund was made.

This will be the loss to Mr S as at that point. To this should be added interest at 8% simple pa from that refund date up to date of settlement following this final decision.

For the additional amount which Mr S withdrew from his ISA, although I understand why Mr S would have been reluctant to withdraw this sum from his pension given the tax situation, I accept that he would ordinarily have done so. But although Mr S needed to withdraw from his tax efficient ISA, it did mean that the funds remained in his tax efficient pension plan. And so to calculate any loss here, Aviva should compare, as at the date of this final decision, the growth on the units withdrawn from the ISA with the growth on the units for the same value in the pension plan. If the ISA units would have performed better, this an additional loss to Mr S.

Mr S has told us that he has fixed protection 2015 in place on his pension so, to avoid any breach of this protection, Aviva should pay any loss to Mr S directly and not into his pension plan.

In addition Aviva should pay Mr S the interest for being deprived of the tax rebated funds at 8% simple per annum from April 2023 to the time he received his refund – as set out above.

I've also considered the matter of compensation here as clearly Mr S has been impacted by the situation over a protracted period. He has suffered the inconvenience of trying to resolve the matter with three different parties and the stress and concern of not knowing when and even if he would get a refund of his lost income. So when looking at the situation overall I think compensation of £250 is fair and reasonable and within the range of what I would consider appropriate in such a situation. So Aviva should also pay Mr S £250.

My final decision

For the reasons that I've given I uphold Mr S' complaint against Aviva Life & Pensions UK

Limited.

Aviva Life & Pensions UK Limited should pay the redress and compensation as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr S to accept or reject my decision before 30 May 2025.

Keith Lawrence
Ombudsman