

The complaint

Mr N has complained that Legal and General Assurance Society Limited (L & G) did not make him aware that taking the benefits from his late father's annuity as a lump sum would cause him to incur a tax charge from His Majesty's Revenue and Customs (HMRC). Mr N would like L & G to reimburse him for this charge.

What happened

I have reviewed all the evidence provided by both parties. I have not reproduced all of this in this decision but concentrated on what I believe to be the most relevant parts.

Mr N's father held an annuity with L & G.. When his father unfortunately passed away in November 2023, L & G wrote to Mr N on 27 November 2023 to explain that he was entitled to some residual benefits from the annuity.

In the letter, L & G explained that Mr N had the choice to take the benefits annually from 2023 until 24 March 2032 or surrender it for an immediate lump sum payment.

The letter went on to say:

Useful tax information

Tax on the pension as income

HM Revenue & Customs (HMRC) say that we must deduct income tax at the appropriate rate from each pension instalment under the Pay As You Earn (PAYE) system. We'll send periodic information showing the tax, if any, that we have deducted.

Tax on a trivial lump sum

The amount of cash which can be paid to you in relation to the guaranteed pension benefit before tax is

[£X]

We must deduct tax from a one-off trivial lump sum using a basic-rate tax code.

Mr N decided to take the benefits as a one-off trivial lump sum payment instead of the annual pension. L & G subsequently made the payment to Mr N and basic rate income tax was deducted from the amount paid.

In September 2024 Mr N received a tax bill from HMRC. It explained that the lump sum payment he had received had been added to his taxable income for the tax year 2023/24. This had resulted in Mr N's taxable income for that year exceeding the basic rate and incurring higher rate income tax on some of his income.

Mr N subsequently contacted L & G on 10 September 2024, complaining that the letter he had received on 27 November 2023 had not made it clear that he may incur an income tax charge at the higher rate.

L&G responded to Mr N's complaint on 26 September 2024. It upheld his complaint, saying:

I agree the letter we sent you on 27 November 2023 didn't give clear information about the possibility of a lump sum pushing you into a higher tax bracket and this may have changed your decision if you'd been made aware.

In recognition of this, L & G paid Mr N £500 compensation.

Mr N was not satisfied with this and contacted L & G on 16 December 2024 to ask it to reimburse him for the full amount of the tax charge as it had admitted it had made a mistake. L & G reviewed Mr N's complaint again and replied to him on 2 January 2025. It did not agree to increase the compensation, saying that in the original options document it provided him:

We advise the lump sum is paid net of basic rate tax.

We also discuss the fact that it may be possible to reclaim some of the tax by contacting HM Revenue and Customs (HMRC). This wording is included at HMRCs request as per their Pensions Tax Manual. They were concerned many people weren't aware they may have paid too much tax and were entitled to a refund.

However, as [Name redacted] acknowledged, we don't know the tax status of the beneficiary and how taking the lump sum may affect them. We can't give specific advice on taxation as we were not regulated to do so. This is why the letter asked you to contact HMRC if you had any questions about tax.

We also asked you to contact us if you had any questions over the content of the letter. If you had contacted us over concerns about your full tax position we could have directed you to HMRC.

Unhappy with this response, Mr N brought his complaint to this service.

Our investigator reviewed all the evidence from both Mr N and L & G, before forming the view that the £500 compensation L & G had paid Mr N was appropriate in the circumstances of this complaint.

Mr N remained unhappy and so the complaint has been passed to me to make a final decision.

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 have reached the same conclusion as our Investigator and uphold Mr N's complaint. I also agree that L & G's mistakes mean that it should pay Mr N £500 in respect of the distress and inconvenience its errors caused him.

I will explain now how I have reached my conclusions.

Firstly, I would like to extend my condolences to Mr N and appreciate that this must have been a very difficult time for him.

I also think it's important to reflect upon the role of this Service. Our role is to impartially review the circumstances of a complaint and make a decision on whether a business has made errors or treated a customer unfairly. Where it has, we expect a business to fairly compensate a customer for any financial loss and distress and inconvenience they have suffered as a result.

In the circumstances of this complaint, I can see that L & G have upheld the Mr N's complaint, so I don't need to decide whether L & G has made a mistake – I need to decide whether the compensation L & G has offered Mr N is appropriate given the mistake it has made. I can see that L & G has offered Mr N £500 in compensation, but he is asking for it to settle his tax bill.

I've carefully considered the letter that L&G sent to Mr N on 27 November 2023. I agree that it could have been clearer in outlining that for some people, such as Mr N, taking a lump sum may result in a higher rate tax charge becoming due.

Having said that, I do find it reasonable to conclude that the letter did make clear that either taking an annual payment until March 2032 or taking the lump sum would be considered as additional income and tax would be deducted from both types of payment and information sent to HMRC accordingly.

The letter states explicitly that income tax would be deducted at the *appropriate rate* from annuity payments or using a *basic rate tax code* from a lump sum payment.

This is because for annual payments, HMRC would instruct L & G how much tax to deduct from each statement. In relation to a lump sum payment, L & G deducted a basic rate of tax as it had no knowledge of how much other income Mr N had in that one tax year. Using a basic rate code ensures that some tax is recovered for HMRC immediately, with the rest, if any to be recovered via Mr N's tax return, as has happened here.

On balance, I think it's fair and reasonable to assume that the letter clearly indicates that both options open to Mr N would be potentially taxable.

In the letter L & G sent Mr N on 2 January 2025, it said

.....we don't know the tax status of the beneficiary and how taking the lump sum may affect them. We can't give specific advice on taxation as we're not regulated to do so. This is why the letter asked you to contact HMRC if you had any questions about tax.

I find that this is correct – L & G cannot give any customer tax advice as it has neither the information nor the necessary regulatory authority to do this. It suggested that Mr N contact HMRC if he had any questions about the tax implications of his choice, which I think is a reasonable approach for it to take, given the constraints it operates under.

In addition, to find that L & G is liable for Mr N's higher rate tax bill I would need to be convinced that he would not otherwise have incurred this bill from the annuity benefits. I've considered that if Mr N had known about the potential tax bill he would incur by taking the lump sum payment, he may well have chosen the annual payments instead. This is, however, a one off choice. If Mr N had taken annual payments, it is entirely possible that his income or any capital gains would have increased his tax bill by increasing his income into the higher rate tax band in one or more years until the payments ceased in 2032.

Having said this, I can fully appreciate that being presented with an unexpected tax bill caused Mr N some significant distress and worry. In considering what level of compensation might be appropriate for this, I have to consider the guidelines that this service publishes to ensure that compensation is appropriate in the circumstances. L & G has offered Mr N the sum of £500, which I feel is in line with the guidelines as well as being fair in the circumstances.

In conclusion, while I fully appreciate that an award of £500 in regard to Mr N's distress and inconvenience is less than he is seeking, I find that it is appropriate in the circumstances of this complaint.

Putting things right

To compensate Mr N fairly, L & G should pay Mr N the sum of £500 in respect of the distress and inconvenience he has suffered, if it has not already done so.

My final decision

For the reasons given above, I uphold Mr N's complaint.

The L & G Mutual Insurance Society Limited should take the actions outlined above to resolve this complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr N to accept or reject my decision before 23 September 2025.

Bill Catchpole
Ombudsman