DRN-4539329

The complaint

Mr H's complaint is about the lifestyle switching on his Scottish Widows Limited pension plan. He says it should have reduced investment risk, but the pension's value reduced dramatically. He says he was misled into thinking his pension was protected, but it was exposed to a single class of investment. And it won't regain its peak value.

What happened

Mr H's complaint was considered by one of our investigators. He sent both parties his assessment of the complaint on 20 December 2023. The investigator didn't recommend that the complaint should be upheld. In summary, the investigator said 'lifestyling' was meant to reduce the risk of investments as a customer approached retirement age. But Scottish Widows never guaranteed it would be protected at its maximum value. The investigator said Scottish Widows had written to Mr H in 2019 when his pension was invested in its mixed fund asking him to review the lifestyling strategy which was based on buying an annuity at retirement.

The investigator said the effect of lifestyle switching was clearly reported in annual statements. And in 2021 Scottish Widows wrote to Mr H's adviser about his pension including its lifestyling strategy. The pension was then invested 45% in the mixed fund, 42% in the protector fund and 13% in cash. No changes were made to the strategy by Mr H or his adviser.

The investigator said since 2022 interest rates had been going up. And that the protector fund was designed to protect value when used to buy an annuity. He said it was mainly invested in bonds which were lower risk than shares. However the value of bonds dropped as interest rates rose. And annuity rates depended on interest rates. So although the protector fund's value may have dropped, this might be offset by Mr H being able to get a higher annuity rate.

Mr H didn't agree with the investigator's findings. He said, in summary, that Scottish Widows had represented lifestyling as a means of protecting his interests as he approached retirement. Events had shown that he had in fact been materially adversely affected as a result of the process. He said as an ordinary investor paying management fees to Scottish Widows, he should be entitled to rely on the representations it made. He said at no point was he made aware of the risks. And had no basis or any reason upon which to make a decision for switching.

The investigator responded to say, in summary, that Scottish Widows didn't make any guarantees about lifestyling. Its aim was to reduce and not eliminate investment risk. He said Mr H's pension funds were already subject to risk. And lifestyling switched his funds from shares to bonds. Traditionally and historically, bonds were considered by the industry to be lower risk than shares. So, in theory the risk should have been lower.

The investigator said although Scottish Widows was paid fees this didn't guarantee the fund's value wouldn't fall. He said Scottish Widows wouldn't be expected to predict the recent rapid rises in interest rates which caused the large fall in the value of bonds – without the benefit of hindsight. He said other events may have caused the original share-based fund to fall. He said he didn't think Scottish Widows had acted unfairly or unreasonably.

Mr H responded to say, in summary, that he had reviewed his pension when Scottish Widows had written to him to do so. Scottish Widows had represented lifestyling as to protect his interests as he approached retirement. So he had no reason to change the lifestyling that Scottish Widows had put in place. He thought Scottish Widows had misrepresented the arrangement.

Mr H said lifestyling had moved funds to a single asset class and this lacked diversification. Even though that asset class was considered safer, it potentially increased the risk since a greater proportion of the fund was exposed to that single risk. He said he accepted that the value of funds wasn't guaranteed, and he had never suggested that it was or that it should be. His complaint was that Scottish Widows had misrepresented lifestyling as a means of tailoring his funds to his pension requirements as retirement approached. He said the evidence clearly showed that that was not the case.

Mr H also said he hadn't suggested that as Scottish Widows was paid fees this meant the value of his funds shouldn't have fallen. He said Scottish Widows was paid fees to manage his funds in a professional manner with due skill and performance. He didn't think it was unreasonable that it should have been aware of the risks as that was what it was being paid for.

Mr H said the investigator had suggested that he might not suffer any financial consequences since the cost of annuities had fallen. He said although this may be correct generally, it didn't seem to be the case for him. But he said even if it was the case, he was still at a huge financial disadvantage because his pensions had large tax-free cash elements - one with an enhanced element. He said Scottish Widows was aware of this, and that it was his intention to take these amounts in full.

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.

I appreciate Mr H's feelings about the matter given the value of his underlying pension fund fell significantly in the years leading up to his retirement date. And this was in the context that he understood the lifestyle approach used to manage his pension lowered the risk as he approached retirement age. However as the investigator said, although the approach was designed to lower risk, it didn't eliminate risk completely. Bonds are broadly considered lower risk than shares. So I think it did lower the risk, generally speaking. But I think what's key in Mr H's particular case is that, as set out in the April 2019 letter from Scottish Widows, his pension was invested in the lifestyle investment strategy balanced investor targeting buying an annuity.

The letter went onto say

Your plan currently has a lifestyle investment strategy based on buying an annuity at retirement. If you think you may choose to take your savings in a different way you should consider changing how your pension is invested.

We've included a booklet which tells you more about your pension and how it's currently invested, as well as the other investment options available to you and next steps if you want to consider making changes.

The protector fund's aim was described as *"to provide a return consistent with the variations in market annuity rates with the aim of reducing annuity conversion risk".* Although bond prices fell sharply, annuity rates correspondingly increased.

I understand the point Mr H has made about lack of diversification. The protector fund was invested almost entirely in bonds. However I think this has to be considered in the context that the lifestyle strategy being employed was targeting the purchase of an annuity. And 25% of the fund was invested in cash. There were also sharp falls in other fixed interest investments that are generally considered to be even lower risk– such a gilts. I think even if the protector fund had significant exposure to such lower risk assets it wouldn't have made a material difference. If Mr H's strategy hadn't been targeting annuity purchase the lifestyling strategy used a different combination of funds.

As I said above, annuity rates have increased significantly over the last few years. What rate of increase depends on what dates are used and what type of annuity is assumed bought. But for example and broadly speaking, since the end of 2021 rates increased approximately 40% (depending on the type of annuity bought) for someone of Mr H's age and at his intended retirement date. So although the fund value may have been lower, the higher annuity rate would usually have meant that Mr H could have bought an annuity providing a similar level of income/benefits.

Mr H has said Scottish Widows was aware he had large tax-free cash elements – and one pension with an enhanced element. He also said it didn't appear that he had benefited from the rise in annuity rates.

Scottish Widows wasn't monitoring the suitability of the strategy for Mr H's *particular* circumstances. It had no responsibility to do so. Scottish Widows alerted Mr H that he was in a strategy targeting buying an annuity, and that he should review whether that was the right strategy for him. I'm not sure why the fund left after taking tax-free cash wouldn't benefit from the significant increase in annuity rates. Ordinarily it should. But as I say, Scottish Widows wasn't monitoring Mr H's particular circumstances. It was for Mr H to decide whether that strategy was right for him. The risk that was being managed was to ensure that, at retirement, any changes to the amount of annuity income Mr H could buy with his pension would be minimised.

Mr H has said Scottish Widows misrepresented lifestyling as a means of tailoring his funds to his pension requirements as retirement approached. He said the evidence clearly showed that that was not the case. However for the reasons I've outlined above, I think the approach *was* tailored, but to Mr H buying an annuity.

I realise my findings will be very disappointing for Mr H. However for the reasons I've set out above and explained by the investigator, I'm not persuaded his complaint should be upheld.

My final decision

My final decision is that I don't uphold Mr H's complaint.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 22 March 2024.

David Ashley
Ombudsman