DRN-4622498

Financial Ombudsman Service

The complaint

Mr M complains that Scottish Widows Limited (Scottish Widows) caused delays in setting up his pension benefits causing him financial losses and distress and inconvenience. He wants compensation for his losses.

What happened

Mr M wanted to take his benefits from his Aviva pension plan. His independent financial adviser (IFA) recommended he take an open market option with Scottish Widows. Where Aviva would pay the maximum tax-free cash sum and transfer the balance to Scottish Widows, who would provide the annuity, which was to be paid monthly in advance. Mr M completed the application form which Scottish Widows received on 15 November 2022 with it would liaise with Aviva. Mr M says he expected the annuity to be set up in November and that he intended to invest his tax-free cash sum in a five-year fixed term deposit account, as was his habit.

But there were multiple problems and Mr M didn't receive his tax-free cash until 9 February 2023. He says fixed deposit rates now had fallen and annuity payments had been missed, as these hadn't started until March 2023. Various complaints had been made about the delays and consequences of them. Mr M said the interest rates now available were 0.65% per annum lower than he could have obtained in November 2022. Causing a loss of around £5,700 over the five years.

Scottish Widows accepted it had caused delays and apologised. It said it took too long to request verification of identity details and hadn't requested the transfer from Aviva until January 2023. And following queries from Aviva didn't receive the funds until 17 February 2023. It said but for the errors Mr M should have been paid his tax-free cash on 2 December 2022, with the annuity starting the same month. It said it had honoured the original annuity rate and paid the missed income payments with interest at 8% per year simple. And had paid interest on the late payment of tax-free cash at the same rate. But it said it wasn't responsible for any future investment loss Mr M might have or for any income tax liabilities. It also paid Mr M a total of £225 in compensation for the distress and inconvenience caused.

Mr M didn't agree with this was fair. And he said the late payments on the annuity had given rise to a 40% tax liability in the 2023/2024 tax year. Which wouldn't have been incurred if paid in the 2022/23 tax year, as he would have paid pension contributions to ensure he remained in the basic rate tax band. He said both he and his wife, who was a potential beneficiary under the annuity, had been caused considerable stress by the delays and uncertainty over what was happening.

Mr M referred his complaint to our service and our investigator looked into it, and she upheld it in part.

Our investigator agreed that Scottish Widows had caused delays. She said she could only consider the impact on Mr M as the complainant rather than on other family members. But she said the compensation paid for distress and inconvenience was too low and it should be increased to £500. But she didn't think it needed to do any more than this.

She said as the annuity application wasn't made until in mid-November, the first annuity payment couldn't have been made until December 2022 by the time funds were received from Aviva, even if there had been no errors. She agreed that Mr M should have been paid his tax-free cash on 2 December 2022. But said the fixed interest account mentioned by Mr M had already reduced the interest rate it offered by the end of November 2022. So, the delay wasn't responsible for this being missed. And as it wasn't clear how Mr M would have invested the funds in December 2022, she thought the 8% interest for late payment paid by Scottish Widows was fair in the circumstances.

She said if Mr M had been paid the correct amount of annuity income between December 2022 and March 2023 it wouldn't create any additional tax liability over what had been expected. And whilst he might have been able to make pension contributions the evidence wasn't sufficient to demonstrate that a higher rate tax liability could have been avoided in the 2022/23 tax year.

Mr M said our investigator had disbelieved his evidence. He said his complaint was not about money but to hold Scottish Widows accountable and our investigator's view just gave it the message to "*carry on doing what you are doing".*

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

My provisional decision

I issued my provision decision on 26 January 2024, I explained the reasons why I was planning to uphold the complaint in part, I said:

I understand the frustration caused by the considerable delays and multiple errors made by Scottish Widows in setting up Mr M's annuity. Having considered the timeline, I agree had it dealt with matters as it should the annuity should have started in December 2022 and made the first income payment then. And that his tax-free cash should have been paid by 2 December 2022.

Compensation for delays

It took Scottish Widows several months to pay the arrears of annuity payments owed to Mr M with this only completed in June 2023. And this was only after repeated complaints from him that it's previous attempts hadn't corrected the errors properly. But it has paid Mr M interest at 8% per year simple to compensate him for being without the use of this income during the delay, which is fair.

It has also paid interest on the late payment of tax-free cash. The amount Mr M received from Aviva in February 2023 was higher than it would have been on 2 December 2022. And Scottish Widows deducted this "extra" amount of around £500 from the compensation it has paid, which Mr M has queried. But this is fair as the aim of the compensation is to put him back in the position he should have been in if there hadn't been any errors. So, it should be based on the sum he should have received on 2 December 2022 rather than the actual payment, whether higher or lower. However, what I think about Mr M's lost investment opportunity, which I consider below, is also relevant here.

Compensation for distress and inconvenience

Scottish Widows has confirmed it has paid Mr M a total of £225 in compensation for the distress and inconvenience caused by the errors and the delays in settling his benefits. I

think that this is insufficient in the circumstances, and this should be increased to £500 in total, a further payment of £275.

Taxation issues

As Mr M notes this is a complex area. He says the delays in the annuity payments gave rise to a higher rate tax liability. And some, or all, of this could have been mitigated by paying pension contributions for himself and his wife (who was his employee) which would have reduced his self-employed taxable profits to below the higher rate threshold.

Mr M says whist the first annuity payment was paid on 1 March 2023, he wasn't aware of that until mid-March 2023 as this wasn't confirmed by Scottish Widows. And he had no time to arrange pension contributions before the tax year end.

But Mr M was advised by his IFA who was chasing Scottish Widows for updates. And it did post confirmation to Mr M that the annuity had been set up on 1 March 2023 and says it emailed the same to his IFA. Given Mr M and the IFA had been pushing Scottish Widows to sort the problems out I think it's reasonable that both would be looking out for these updates.

But for the delays Mr M had expected the annuity would be set up in November 2022. And the payments expected within the tax year were always likely to result in a higher rate liability. So, if Mr M wanted to mitigate higher rate tax liabilities, I think it's reasonable that some investigation and consideration of this would have been undertaken before March 2023. And there would have still been time to make the necessary additional contributions before the end of the tax year reflecting the actual payments received. So, I don't think it is reasonable to hold Scottish Widows responsible for these tax issues.

Mr M says having purchased the annuity his scope to pay pension contributions has reduced to £10,000 per year. Limiting his opportunity to mitigate the "extra" tax on the late payments paid in the 2023/23 tax year. I don't have details of any other pension benefits Mr M may have accessed, which may be relevant. But purchasing a conventional lifetime annuity, as I understand the arrangement with Scottish Widows to be, wouldn't normally result in the application of the Money Purchase Annual Allowance. Which limits tax relievable pension contributions to £10,000 per year. He may wish to check this with his IFA.

Lost future investment return

Mr M says he lost the opportunity to secure higher five-year fixed term deposit rates due to the delayed payment of his tax-free cash. When a business's error has prevented or delayed an investment being made, we do consider it fair and reasonable that any identifiable losses be made good. Because that puts the client back into the position they would have been in but for the error.

However, it is important to avoid the use of hindsight which could be obviously unfair. So, it's necessary that there be reasonable evidence of what someone intended to do but couldn't because of the error. Mr M has noted that he couldn't make the investment until he had the funds and that it was his habit to invest in longer term fixed rate deposits. He also says he discussed his intentions with his IFA in November 2022 and any further detail about this would be helpful if he can provide it.

And there was an email from Mr M to his IFA on 10 February 2023 where he set out details of a fixed rate account that was available in November 2022. This offered 5.05% per annum, fixed for five years. He said the accounts then available (10 February 2023), only offered around 4.3% per annum. And as his tax-free cash sum was over £160,000, his losses would be around £6,000 over five years.

Scottish Widows said it wouldn't consider this loss and that 8% interest on the delayed payment was fair. And our investigator said the rate Mr M had mentioned had actually reduced during November 2022 and a lower rate was on offer by 2 December 2022. So, as it wasn't clear exactly what account Mr M would have invested in, she felt it wasn't reasonable to hold Scottish Widows responsible for this.

However, having considered this carefully I think there is adequate evidence of Mr M's intentions. And if he has suffered a loss, he should be compensated for it.

Deposit accounts are simple investments with the prime consideration being identifying the best interest rate on offer for the duration required, at the point the investor has the funds to open the account. Banks do change the rates offered at short notice. This was certainly the case in November/December 2022, with longer fixed term rates declining even though the Bank of England was continuing to increase Base Rate. That means that Mr M may well have identified Bank A on a preliminary basis only for Bank B to be offering a better rate the next day. So, I'd expect that once he received the tax-free cash, he'd check for the best rates then available.

And within days of receiving his tax-free cash Mr M went ahead and invested virtually all of it in five-year fixed rate deposit accounts with two different banks. I've no reason to think he wouldn't have done the same in December 2022, when Scottish Widows accepts he should have received his tax-free cash.

It seems to me, that a factor influencing Mr M's decision to take his pension benefits, despite him continuing to work, was that interest rates had increased significantly. That meant both annuity and deposit rates were the highest they'd been for many years. Purchasing an annuity locks into the prevailing, and at the time, relatively high rate for life and a five-year fixed rate deposit account is akin to that.

Mr M says he identified the best accounts by researching the market at the time online, but he hasn't been able to provide records of his online searches. I think this "lack" of physical evidence however somewhat supports his testimony that he had researched the market at the time rather than with the benefit of hindsight in February 2023. I say that because having carried out an internet search myself, it is difficult to obtain specific information about historical rates offered by specific banks. But Mr M was able to provide specific details of a bank and the interest rates it had offered in November 2022, when he'd expected his tax-free cash to be paid. Which again suggests that it was his intention to invest his tax-free cash sum in this manner.

But there are published sources of information about the deposit accounts available in December 2022, and they do appear to be superior to the rates Mr M secured in February 2023. And an article from The Times on 10 December 2022 titled, "Savings rates aren't getting any better – grab that 4.9% deal now", referred to five-year fixed rates "of nearly 5 per cent". So, rates of nearly 5% appeared to be available from several banks at the time. Both Mr M and Scottish Widows may want to obtain further evidence around this.

So, I think it is reasonable that a comparison is made to the rates available in the first week of December 2022 to those actually secured by Mr M in February 2023. He deposited £83,000 into two different five-year fixed rate accounts. One offered 4.35%, the other 4.5%. So, his average return is 4.425% per annum over five years before tax.

As rates had reduced through November 2022, the difference between what Mr M did secure and what was available in December 2022 may not be as great as he initially thought. And is perhaps around 0.4-0.5% less per annum. Scottish Widows has however

already paid him interest at 8% per year simple on the delayed payment of his tax-free cash of £1,482.05 net of basic rate tax, which would need to be considered in any calculation of loss. I haven't completed calculations, but it does seem likely Mr M has still suffered a loss through not being able to secure the rates available in December 2022.

Putting things right

I set out how I thought Scottish Widows should put Mr M back in the position he should have been in if he'd been able to invest in two leading five-year fixed rate deposit accounts on 6 December 2022 rather than in February 2023.

In summary, I said Mr M and Scottish Widows should agree the appropriate interest rate and compare this to the actual average rate Mr M did secure, allowing for the increased tax-free cash payment and any compensation it had already paid in respect of the late payment of this. And if the calculations showed a loss, it should pay it to him.

And I said I thought Scottish Widows should pay Mr M a further £275 in compensation for the distress and inconvenience he has suffered as a result of its error to give £500 in total.

I asked both parties to send me any further information or comments they would like me to consider.

Response to provisional decision

Scottish Widows accepted my decision. It queried the average interest rate Mr M had obtained, which it said was 4.375%. It said it had made enquiries and considered a fair rate for the loss calculation to be 4.56%. It showed evidence that Tandem Bank (who Mr M had initially had in mind) offered 4.65%. But it provided no evidence of the other rates it used to arrive at its average of 4.56%, which it said were as at 22 December 2022.

Scottish Widows had carried out calculations based on that 4.56% average. These allowed for the "additional" tax-free cash paid and the interest already paid for late payment. The calculations showed there wasn't an overall loss on the five-year fixed rate deposits, so it said no further compensation was due.

I asked that these calculations be sent to Mr M for his comments.

Mr M agreed in part with my decision and agreed the average rate he'd secured was 4.375%.

But he didn't agree with the average interest rate of 4.56% proposed by Scottish Widows for the loss calculations. He said this was too low, as 4.9% was available from Shepherds Friendly in the first week of December 2022. But he said he hadn't been able to locate his notes of the other rates available at the time.

Mr M disagreed that it was right for the 8% interest already paid to be allowed for in these calculations, as this was for the late payment not the subsequent loss of interest. He said doing so meant there was *"no financial penalty against"* Scottish Widows and no *"incentive"* for it not to just carry on as before.

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.

I don't think Mr M was treated fairly as Scottish Widows caused unreasonable delays in the settlement of his benefits. It has generally addressed the losses caused by this. But I think it is fair that Mr M should also be compensated for any investment loss he may have been caused as a result of the delays in receiving his benefits. Scottish Widows has also paid some compensation for the distress and inconvenience it has caused Mr M, but I think in the circumstances here, this should be increased.

Mr M has queried how I'd proposed the potential losses should be calculated, saying it didn't penalise Scottish Widows or adequately compensate him for his loss.

However, our service doesn't regulate financial firms, which is the role of the Financial Conduct Authority. Our role is to resolve complaints impartially by being fair to both sides. So, I can't punish a firm for making errors or tell it to change its systems and procedures. But I can tell it to pay compensation for losses suffered, and I can award compensation for any distress and inconvenience caused. And when we tell a firm to make good a loss the aim is to put the consumer back into the position they would have been as if the error hadn't been made, we don't award punitive damages.

Mr M's complaint is that he has suffered a loss of future investment return because interest rates fell whilst Scottish Widows delayed payment of his benefits. To put him back into the position he should have been in, it's necessary to consider what the investment return should have been compared to what actually happened. Had there been no error, Mr M would have invested a slightly lower sum at a higher interest rate for the next five years from December 2022, and he wouldn't have received any interest from Scottish Widows for late payment.

So, any increase in the tax-free cash sum and any interest already paid for late payment (itself reflecting the lost return during the delay) does need to be considered in any further calculation or too much compensation could be paid which isn't fair to Scottish Widows.

Unfortunately, there hasn't been agreement about what interest rate Mr M could have secured in December 2022. But there is evidence that a rate of 4.9% was available from Shepherds Friendly for a comparable account. So, higher than the rate evidenced by Scottish Widows from Tandem bank of 4.65%. Savings rates were being reduced frequently through November and December 2022. I think the 22 December 2022 date Scottish Widows has referred to, is too late for a fair comparison. As I think Mr M would have invested in the first week of December 2022 had his fund been paid when they should have been.

As I explained in my provisional decision, I think Mr M would have accessed the highest rates and divided the investment of his tax-free cash between two deposit takers to remain within the FSCS compensation limits. So, I think it's fair that the average of these two rates identified above should be used in the loss calculation, which is 4.775% rather than the average rate of 4.56% Scottish Widows has used so far.

Putting things right

My aim in awarding compensation is to put Mr M back in the position he would have been in but for the errors. So, Scottish Widows must:

- Re-run its calculations of the total interest earned assuming the five-year fixed rate accounts had been opened in December 2022 with an average interest rate of 4.775%.

- Compare this to the total interest that will be earned on the average interest rate of 4.375% Mr M obtained on the actual five-year fixed rate accounts he opened on 10 and 13 February 2023.

- It may allow for the increased value of the tax-free cash and the late payment interest it has already paid on this.

- If the final calculation shows Mr M has suffered a loss, Scottish Widows must pay that sum to him.

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

- It must provide Mr M with a simple calculation of how it arrived at the final figures.

- Scottish Widows must pay Mr M a further £275 in compensation for the distress and inconvenience he has suffered as a result of its error to give £500 in total.

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 Scottish Widows Limited.

I direct Scottish Widows Limited to undertake the calculations set out above and pay any compensation due to Mr M.

I further Scottish Widows Limited to pay Mr M an additional £275 in compensation to give £500 in total for the distress and inconvenience he has been caused.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 13 March 2024.

Nigel Bracken
Ombudsman