DRN-4656154

The complaint

Mr K complains that Aviva Life and Pensions UK Limited (Aviva) underpaid his quarterly annuity payment in March 2020.

What happened

Mr K is unhappy that the annuity payments from his variable annuity held with Aviva have been calculated incorrectly. His payments have been made quarterly since 1997. In March 2020 his quarterly payment was a lot lower than his previous annuity payments and payments he has received since.

Mr K raised a complaint with Aviva in April 2020 about the sudden reduction to his quarterly payment. He said this payment had been made without any prior warning or explanation. And that this had caused him extreme anxiety and inconvenience.

Aviva issued its final response to the complaint on 15 June 2020. It said that the decrease was due to market conditions. It paid Mr K £50 for the inconvenience it felt its delayed response had caused him.

Mr K wasn't happy with Aviva's response. He said it'd issued a quotation to him on 27 February 1997 which had stated: "*that the broad effect of the plan is to invest in a Fund which is confined to the Stock Market and is thus liable to fluctuation. However, because the Company has "a skilled and experienced staff who have the benefit of the advice of expert financial consultants, the fund is expected in the long run to prosper and bring substantial benefits to all policyholders. A "smoothing process" is employed to average highs and lows*."

Mr K said that he'd only been paid £2,776.36 in March 2020 compared with £5,395.98 in 2019, £5,029.07 in 2018 and £5,053.68 in 2017. He felt that Aviva had either failed in its management of the fund in the first quarter of 2020, or had miscalculated the payment. He asked it to review its response so it could offer him fairer compensation.

Aviva investigated further and replied to Mr K on 21 August 2020. It said that it had found that rises and falls in the market had been amplified in its calculation of income. It confirmed that it would need to investigate further to understand the full impact this had on Mr K's income and would be in touch once it had completed the investigation.

Mr K was unhappy with this response. So he brought his complaint to this service. He said his complaint concerned solely the March 2020 payment which he felt had been reduced to a level entirely out of proportion to the decline in market values. He felt this had led to an underpayment in March 2020 of approximately £2,000. Mr K said that Aviva had yet to calculate his loss, and therefore it hadn't compensated him financially.

Aviva confirmed to this service that it hadn't completed its investigations. So it didn't know if Mr K had suffered a financial loss. It said it intended to complete its investigations and the work to rectify any issues found by August 2021.

In May 2021, our investigator upheld Mr K's 2020 complaint. She felt that it had taken a long time to resolve the issue, and noted that the review was yet to be completed. So she considered that Aviva should pay Mr K £500 for the trouble and upset the error and the time taken to investigate the error had caused him. She also felt that if the review showed that Mr K had lost out, Aviva should pay Mr K financial compensation to put him back in the position he would've been in if the error hadn't occurred.

Aviva agreed with our investigator and arranged to pay him the recommended £500 trouble and upset compensation.

In August 2021, Mr K told this service that he still hadn't received financial compensation for the underpayment he felt Aviva had made in March 2020. He asked this service to get Aviva to specify the amount of the underpayment and to give a firm date for settlement with interest.

I understand that Aviva completed its calculations in September 2021. It wrote to Mr K on 20 September 2021 to tell him there'd been no financial detriment to him. It said that it had significantly overpaid him over the last decade, but that it wouldn't be asking him to repay any overpayments. It also said that this applied to the majority of variable annuity customers.

Aviva said that the fund Mr K was invested in didn't track any particular index, and that the investment strategy wasn't to achieve returns equal to or in excess of any specific index. It also said that the fund income was directly impacted by the dividends paid out by UK companies, the vast majority of which had been stopped or deferred when the unit price was calculated for the March 2020 payment.

Aviva also said that as a result of the review, it felt that the overly-variable nature of annuity payments had been an issue for customers, particularly during March 2020. So it had taken steps to reduce the volatility of annuity payments in the medium and long term.

Mr K said he couldn't accept Aviva's confirmation that he'd suffered no financial detriment without any independent audit to confirm its actuarial calculations. He still felt that Aviva had an obligation to refund with interest the underpayment of his quarterly annuity made in March 2020.

Aviva responded on 8 November 2021 to confirm that Mr K had received significant overpayments on his annuity, which it wouldn't try to recover. It acknowledged that he may have had a loss of expectation about the amount of his annuity payments. But confirmed that he hadn't suffered a financial loss.

Mr K repeated to Aviva that his complaint remained that he felt he'd been underpaid by around £2,000 in March 2020, on the basis that Aviva's calculations for March 2020 were consistent with its calculations from June, September and December 2020. Mr K said that Aviva had failed to produce any actuarial evidence in support of its calculations. Nor had it provided him with an auditor's report in evidence.

Mr K asked this service to press Aviva to make the compensatory payment he still felt it owed him. He said that it had still failed to provide him with any actuarial evidence.

Our investigator raised a new complaint with Aviva in February 2022 about the financial calculations it had carried out in respect of Mr K's original complaint.

Mr K said this wasn't a new complaint. He confirmed that his complaint was still that the annuity payment of 30 March 2020 had been miscalculated and then he'd been underpaid about £2,000.

Our investigator told Mr K that Aviva had completed its investigation and found that there had been no financial loss. She said that as Mr K was unhappy with the outcome of Aviva's investigation, and had requested an auditor's report, this would need to be looked at as a new complaint.

Mr K felt that there'd been some confusion. He said his complaint was about his individual annuity, and the low March 2020 quarterly payment. He felt that Aviva had admitted it had miscalculated the degree to which the market value of the fund had fallen and promised to recalculate actuarially the value which should be repaid. But he said he'd never received this information.

Mr K said he didn't agree with Aviva's claim that the specific underpayment in March 2020 was connected to a separate general actuarial error for which it had said it wouldn't claim adjustment from policyholders.

Aviva replied to Mr K in October 2022. It said it hadn't promised it would provide him with an actuarial or auditor's report. It confirmed that Aviva's profits as a company didn't impact the variable annuity fund in which Mr K was invested. And said that its review had confirmed that these issues it'd found applied to all its variable annuity customers, not just Mr K.

Aviva said the variable annuity didn't provide any guarantees that the quarterly payments would be consistent with previous payments or that they would always rise in value. And that the unit price wasn't linked to any inflation index, or any specific market index, so there was no guarantee that rises or falls would mirror any particular index.

Aviva also confirmed that Mr K's March 2020 payment hadn't been underpaid. It said it had been based on the correct calculation. It said that as the actual calculations were commercially sensitive, it couldn't share them with Mr K. But said he could access information about the fund, its performance and the fund managers reports on its website at any time. It also said that it would be monitoring its calculations to ensure that they continued to be fair and consistent.

Mr K said that while his original claim was that he'd been underpaid around £2,000 in March 2020, he was prepared to accept an immediate payment of £1,500.

Aviva wrote to Mr K again on 9 January 2023, although he said he didn't receive this letter. It said there were no further actions or payments for it to complete the matter.

Aviva wrote to Mr K again on 4 April 2023. It acknowledged that he'd reduced the amount of his claim to £1,500. But said that the amount requested hadn't been the reason it'd rejected his claim. It said that if any income had been lost, it would have arranged a payment to cover the difference, no matter the value.

Aviva said that since its investigation into the payments, a full review of the variable annuity product had taken place. It said that it had found a further issue regarding mortality rates. It said that it hadn't historically reviewed the assumptions it used about longevity as frequently as they should've been. And that this could mean that annuity payments could've been higher or lower than intended.

Aviva said it was investigating this issue by revisiting the entire history of annuity payments to all customers since 2001. And that it aimed to complete this review in the next couple of months. And that if the net effect of its review was that any annuitants had been underpaid overall, it would write to them and make a remediation payment for the loss of income.

Mr K replied to Aviva. He said he'd never disputed the values of the quarterly annuity payments made before or after that of March 2020. So he didn't think that Aviva's 4 April 2023 letter was relevant to his outstanding complaint. He still felt that Aviva owed him about £2,000 in respect of the March 2020 payment.

Aviva told this service that the review it had outlined in its 4 April 2023 letter was taking longer to complete than it had expected.

In July 2023, our investigator set up a new complaint for Mr K.

In September 2023, our investigator told Mr K that she was still investigating his complaint but due to the new related issue she'd set up a new case. She also provided him with the latest update from Aviva, which said that although it hadn't completed its calculations, it appeared that Mr K hadn't suffered any detriment from the new issues, but had benefited from overpayments which it wouldn't ask him to repay. It also said that it would write to Mr K separately to provide an update.

Mr K was unhappy with what our investigator had told him. He still felt that there was no new issue related to his original complaint. He reiterated that his complaint was that his March 2020 annuity payment had been considerably lower than was to be expected given the market conditions at that time.

Mr K said that the only issue remaining was for Aviva to agree a value for settlement of the March 2020 underpayment.

Our investigator told Mr K that she understood his complaint was that he'd been underpaid in March 2020. She said she'd asked Aviva for a breakdown of the calculations to see when Mr K had been overpaid and by how much so she could confirm whether there had been a loss. But that while she'd been waiting for that information, Aviva had identified a further issue with the calculations of Mr K's income which it was in the process of reviewing. And that this could change the outcome of Aviva's previous review into Mr K's income amounts.

Our investigator told Mr K that while she understood his frustration at the delay, she couldn't ask Aviva to pay compensation for a financial loss without evidence that there had been a loss.

Mr K still felt that the March 2020 payment was out of line with previous and subsequent payments. He felt there'd been an underpayment due to an arithmetical error. He wanted our investigator to address this with Aviva.

Aviva wrote a holding letter to Mr K on 5 December 2023 to tell him that its specialist payments teams were reviewing his policy and in particular the payments he'd received to identify whether there had been an underpayment. It apologised for the delay and said it had arranged for a payment for £500 to be paid to Mr K.

Aviva issued a further final response letter to Mr K on 21 December 2023. It said its actuaries had now completed their calculations. And that these showed that there had been an error in calculating the unit prices historically.

Aviva said that the unit price depended on both the investment return achieved by the fund and the life expectancy of all customers that may be eligible for payments in the future. It said it had found an error in 2008 which meant that life expectancy of customers was being underestimated, and that this would've led to the fund running out of money meaning that future annuity payments couldn't be made. It said it had also found that the unit price wasn't increasing when customers died earlier than expected. And that the net effect of these issues meant that Mr K had been underpaid by a total of £7,675.24 between March 2001 and December 2009.

Aviva said that at the end of 2009, additional money was added to the fund to ensure that all future payments could be fulfilled. But that the life expectancy issue hadn't yet been properly resolved, so the unit price calculations continued to underestimate life expectancy. It said that the fund injection and this underestimation caused investment returns to be inflated and paid out sooner than anticipated. And that by 2020 this had caused the change in unit price to be roughly double the return on the assets backing the fund. It said that because the fund had produced consistently positive returns between 2009 and 2019, the unit price increased to a much higher level than it should've been. So the difference between the annuity payments that Mr K had received and the amount that he should've received kept increasing. This had led to him receiving his biggest overpayment in December 2019 when he was paid £6,081.81 instead of the correct £2,811.76. It said that after this December 2019 payment, Mr K had been overpaid a total of £49,836.31, which took into account the £7,675.24 of underpayments.

Aviva explained that its error in calculating the unit price also meant that if the fund decreased by 1% the unit price would decrease by around 2%. It said that Mr K had queried his March 2020 payment as it had fallen from £6,081.81 in December 2019 to £2,776.36, a decrease of 54%. It said that the fund had fallen by approximately 25% over the first quarter of 2020, and that this had been amplified to the 54% decrease in his annuity payment due to the unit price calculation issue. It said that this payment had still been higher than it would've been if the correct unit price had been used to calculate all of his payments. Aviva said that Mr K should've received £2,116.14 in March 2020 which would've been a 25% fall compared to the correct £2,776.36 December 2019 payment and this decrease would've been in line with the market fall.

Aviva also said that in total Mr K had been overpaid by £86,326.44 between March 2001 and September 2023. It said its calculations used a complex model to ensure that all factors had been considered and analysed. And that the model had been thoroughly checked, so it was confident that all of the figures were correct.

Aviva also said that it didn't intend to fix the unit price by reducing it to the correct level. And that the issue had now been fixed so Mr K's annuity payments would reflect both the investment returns of the fund and the age profile of the remaining annuitants going forward. It also confirmed that it wouldn't be asking for any of the overpayments to be returned.

Mr K replied to Aviva on 14 January 2024. He maintained that he'd been underpaid in March 2020. He said he was prepared to accept an additional £1,300 to settle the issue.

Mr K also wrote to Aviva on 15 January 2024 after receiving its 21 December 2023 final response letter. He said that his variable annuity had started in 1997 with a quarterly payment of £1,788. He felt that this was bigger in real terms than the low values Aviva now attributed to December 2019 and March 2020. He felt it was incredible that errors of such magnitude should've escaped the notice of professionals such as auditors, actuaries and financial advisers.

Our investigator didn't think that Aviva needed to take any further steps to put things right. She acknowledged that Aviva had taken a long time to complete all of its investigations. And that Mr K had suffered a loss of expectation as his payments had reduced from the higher level he'd got used to. But she said Aviva had overpaid Mr K by a total of £86,326.44 between March 2001 and September 2023, which it'd confirmed it wouldn't reclaim.

Our investigator said she couldn't say that Aviva had caused Mr K a financial loss in March 2020. She said this was the correct amount. She also felt that the compensation for the trouble and upset the delays had caused was fair.

Mr K still felt that he'd been underpaid in March 2020. He felt that our investigator should've waited for Aviva's response to his request for a further £1,300 of compensation before she'd issued her view.

Our investigator maintained that Mr K had been overpaid both in March 2020 and overall. And that he hadn't suffered a financial loss.

Mr K wrote to Aviva to say that he was satisfied that all quarterly payments made after the inception of the policy and up to December 2019 were correctly calculated at the values paid and not at the lower values which Aviva had outlined. He said that if it disagreed, it should refer the facts to the Institute of Actuaries so that it could verify the calculations.

Mr K also told this service that his only complaint was that the quarterly payment of March 2020 should've been calculated in accordance with his contract of March 1997. And that he had completely rejected Aviva's statements in its 22 December 2023 letter. He said he didn't accept that his policy was miscalculated from the start with reference to his life expectancy. Nor did he agree that his annuity payments were undervalued in the past.

Mr K said he wanted an additional payment of £1,000 and a promise that his future payments would be calculated in accordance with his unit holdings in the fund. He also wanted Aviva's calculations to be independently verified by the Institute of Actuaries.

As agreement couldn't be reached, the complaint has come to me for a review.

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'm not going to ask Aviva to take any further steps to put things right. I know this will be disappointing to Mr K. But I'm satisfied that he's not suffered a financial detriment because of Aviva's errors. I'll explain the reasons for my decision.

I first considered Mr K's request for Aviva's calculations to be independently verified.

Can I require Aviva to get its calculations independently verified?

I'd like to explain this service's role. We're an informal dispute resolution service. We can't check calculations of the sort Aviva's actuarial department has carried out in answering Mr K's complaint. Nor, under the circumstances of this complaint, can we fairly require Aviva to get its calculations independently checked by the Institute of Actuaries, as Mr K requests.

Aviva told Mr K in October 2022 that it hadn't promised it would provide him with an actuarial or auditor's report. And I've seen no evidence that it's required to do so.

There are a number of reasons for my view here. For one, Aviva's calculations have already been carried out by experts and have been thoroughly reviewed. So there's no reason to doubt them. Aviva has also explained that the calculations are commercially sensitive. Therefore it's unable to share them for a third party to review. I consider this to be a reasonable stance.

I next considered whether Aviva has paid Mr K quarterly annuity payments in line with his contract.

Have the annuity payments been high enough?

I acknowledge that Mr K doesn't dispute any of the quarterly annuity payments that have been made to him other than that of March 2020. And that he feels that there'd been an underpayment due to an arithmetical error.

I also acknowledge that Mr K completely rejects the contents of Aviva's 22 December 2023 letter. But, as I stated earlier in my decision, there's no evidence to suggest that the calculations in that letter are incorrect.

The letter explained that the errors Aviva had identified had led to Mr K receiving his biggest overpayment in December 2019. It said it'd incorrectly paid him £6,081.81 when it should've paid him £2,811.76 at this point. It also explained that its error in calculating the unit price meant that if the fund decreased by 1% the unit price would decrease by around 2%. And that this was the reason that the March 2020 payment had fallen by about 54% instead of around 25%, as Mr K had calculated. Aviva said that the March 2020 payment had still been higher than it would've been if the correct unit price had been used to calculate all of Mr K's payments. It said it should've been £2,116.14 rather than the £2,776.36 it'd paid him.

Therefore I'm satisfied that Mr K has financially benefited from Aviva's errors overall. And that, specifically, the March 2020 annuity payment at the centre of his complaint was considerably higher than it would've been if it had been paid in line with his contract from the start. Therefore I can't reasonably agree with Mr K that all of the actual annuity payments made to him up to December 2019 were correct. And that Aviva underpaid him in March 2020.

I've also reviewed the terms and conditions for Mr K's policy. The relevant section here is Section 12, Value of Annuity Units.

Aviva has also confirmed that the unit price for its variable annuities comprises a future growth assumption and the longevity of all annuitants, and that it is not simply an accumulation of investment returns. It said it uses this method so that each annuity payment is the maximum amount possible while ensuring that all future annuity payments can be made to all policyholders which have the variable annuity product.

I do acknowledge that the letter Aviva sent Mr K dated 27 February 1997 with his variable annuity quote didn't explain the calculation method in full detail. That letter stated:

"*In the case of the variable annuity, your entitlement is stated in a certain number of annuity units, rather than in an amount in pounds. For instance, if you chose to receive a full variable annuity out of the enclosed quotation, every instalment of the annuity would be calculated as follows:*

Quarterly allocation of annuity units X annuity unit price = Gross payment

The annuity unit price changes on a weekly basis, and it may go up or down."

But the terms and conditions of the policy always required the longevity of all the annuitants to be taken into account as well. Therefore, although the 27 February 1997 letter could've been clearer, the terms and conditions correctly reflect the required calculation.

I also acknowledge that Mr K feels that Aviva didn't take account of his own changing life expectancy, in respect of its admission of using incorrect longevity data for all annuitants. He felt that his original quotation was based on: "*a disability free life expectancy of what I believe to have then been eighteen years*", but that when he'd reported to Aviva in

December 2020 that his health had worsened, it'd told him that this didn't present grounds to alter the calculation of the annuity. But I need to make it clear that Aviva bases its calculations for the variable annuity payments of all its policyholders on the longevity of all annuitants, which I understand it takes from wide-ranging data not limited to its own experience, and certainly not based on the experience of a single policyholder. So I'm satisfied that it didn't do anything wrong in this regard.

I next considered if the compensation Aviva has paid Mr K for the trouble and upset it's caused him was fair.

Trouble and upset

It's clear that this matter has had a significant impact on Mr K. It must've been very worrying to receive a much lower payment than he was expecting in March 2020, without any explanation or advance warning.

The whole process of checking whether Mr K had been underpaid or not has also been a long one, with other errors being picked up by Aviva along the way which have caused further delays and confusion.

Aviva has paid Mr K a total of £1,000 for the trouble and upset this has caused.

Aviva's calculations have also showed that Mr K is financially considerably better off as a result of its errors.

Having carefully considered the overall complaint, I'm satisfied that Aviva has paid Mr K sufficient trouble and upset compensation under the circumstances.

Aviva has provided further details about what it's done to ensure Mr K hasn't lost out. As I noted earlier, we aren't able to offer an auditing service to check calculations. But I've looked at its explanation, and I'm satisfied that Mr K hasn't suffered a loss either overall, or in the specific case of his March 2020 annuity payment.

Therefore I can't reasonably ask Aviva to make an additional payment of £1,000, or to take any further steps to put things right. I do however of course expect Aviva to ensure that Mr K's future payments will be calculated in accordance with the terms and conditions of his policy. I can see that Mr K has spent considerable time on this complaint over the last four years. I hope that he can now put this complaint behind him.

My final decision

For the reasons I've set out above, I don't uphold this complaint.

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

Jo Occleshaw
Ombudsman