

complaint

Mr R complains about compensation paid to him in 2016 relating to his section 32 pension plan. Aviva Life Services UK Limited ('Aviva') has accepted it could have paid his annuity from the plan when he was age 60. He had wanted to receive annuity payments within his overall personal tax allowance and not pay income tax. As a result he had to go out to work for five more years to replace the foregone annuity payments. But having now received these in a lump sum, he has incurred a tax liability he would otherwise have avoided.

background

Mr R had a section 32 plan with Aviva. He received a pre-retirement pack just before he was due to take benefits in 2011 at age 60. He was aware of how much his annuity might be and planned to take the income, retire, and plan his overall finances to ensure he paid very little income tax until his state pension began at age 65.

A year later Aviva advised Mr R that he couldn't take the benefits from the plan because the guaranteed minimum payment (GMP) couldn't be supported from the fund at that time. Mr R decided he needed to replace the income he was due to receive from the plan so he returned to work as a locum pharmacist.

Over the next five years Mr R tried to earn a level of income that meant he paid little or no income tax. However, in 2016 Aviva said it had made an error in not paying him his annuity in 2011 and paid compensation of around £21,000. It deducted basic rate tax from the compensation lump sum as the amount was above Mr R's personal tax allowance.

Mr R complained as he felt he'd only had to work for those five years because Aviva said it couldn't pay him. And he wouldn't have had tax deducted from the annual annuity payments as he would have ensured his income would have been below the tax threshold, as had been the case with his earned income. But Aviva said it couldn't refund the tax according to HMRC rules but did offer £500 for the inconvenience he'd suffered in having to go to work for an additional five years.

One of our adjudicator's investigated the complaint and said he thought it should be upheld. He said that the evidence he'd seen did show that Mr R had managed to work few enough hours to remain below the tax threshold and he was satisfied that had Mr R received his annuity payments as he should have done, he probably wouldn't have paid tax on them.

He considered that Aviva should have considered the implications of its error and didn't think the £500 was an appropriate amount of compensation. He said that it wasn't possible for Mr R to get a refund of the tax from HMRC, so he recommended that Aviva should compensate Mr R for being financially disadvantaged. He recommended that Aviva paid £1,000 for each year Mr R had to go to work which was a total of £5,000.

Aviva did not agree. It said the amount recommended was too high and beyond what it had paid other clients who had suffered from the same error. It offered a further £100 for any inconvenience Mr R had suffered in dealing with HMRC, but believed Mr R had benefitted from the income he'd received from working and would probably have paid tax anyway.

The adjudicator didn't change his view but said that Mr R *had* demonstrated that he didn't pay income tax when he worked for the five years.

As agreement was not reached the matter has been referred to me.

my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint. Having done so, I have come to the same conclusions as the adjudicator and for broadly the same reasons. I have though decided an alternative redress solution would be appropriate.

Aviva has accepted that when it was made aware that it could have provided annuities which covered the GMP within section 32 plans, it reviewed any plans that were affected and offered compensation for the missed annuity payments. In line with HMRC guidelines it taxed the payments accordingly. That would seem to have been a reasonable way of resolving the situation.

However, Mr R had a financial strategy which involved him retiring at age 60 and incorporating the annuity payments from his Aviva plan. As he was aware of the amount involved, and had significant other tax free lump sums that he could use to fund his retirement, he said he could ensure his income remained below his tax allowance threshold. Instead Mr R had to go to work for five more years' in order to provide that missing income when Aviva said it couldn't pay him.

I've looked at Mr R's tax returns for the years concerned. It's clear that, with the exception of the first year, he did just enough work to ensure he paid little or no tax. I'm satisfied therefore that Mr R did have a strategy which would ensure he paid the minimum of income tax.

Based on that information I think it's most likely that, as he knew the annuity payment he was going to receive at age 60 which was sent to him in his pre-retirement pack, he could have arranged his finances including the annuity payment to ensure he didn't pay tax.

Like the adjudicator I am not persuaded Aviva has fully recognised Mr R's circumstances and the financial plan he had established that was conditional on the annuity payments, and then the additional earned income when the annuity payments couldn't be made.

I am persuaded Mr R would have enjoyed an income below the basic rate tax threshold. It follows I am persuaded that he has been financially disadvantaged by both paying income tax on the compensation and by working for a further five years when he hadn't planned to.

Aviva says Mr R has enjoyed the extra income he received and that HMRC might be able to "*spread out*" the tax liability over the five years. That may be the case; but Mr R has been put to considerable inconvenience through no fault of his own. I don't believe Mr R set out to get extra income by working in the 5 years of missed annuity payments. I am persuaded by the evidence I have seen that had he received the annuity payments to which he was entitled, he would not have taken on the work he did. I believe he undertook this work in order to replace, rather than supplement the (tax free) income he had expected in 2011.

For those reasons I agree with the adjudicator that Aviva should compensate Mr R. The adjudicator suggested to Aviva that an appropriate sum would be £5000 in addition to the £600 it has already offered. This was £1,000 compensation for each year that he had to continue working as a result of Aviva's error.

Aviva disagreed saying that such a 'blanket' sum was excessive. I have carefully considered this. In doing so, I revisited the redress calculation Aviva applied in paying Mr R the 'missing' annuity payments in August 2016. In my view, it had applied an excessive tax charge to the redress and applied a lower interest rate than this service uses in compensating consumers where a complaint is upheld.

I provisionally concluded an alternative redress solution was preferable both in terms of fairness and transparency. Accordingly, I asked the adjudicator to inform Aviva of my proposed redress. Aviva did not agree with the sum that resulted from my proposed solution.

But it did then agree that Mr R should be compensated. It said any compensation should reflect the potential for Mr R to reclaim from HMRC some of the tax he incurred as a result of Aviva's error. But it agreed an interest rate of 8% should apply to the missed annuity income.

It offered Mr R £4048.65 and increased its distress and inconvenience payment from £600 to £700. In total, its new offer amounted to £4748.65. Mr R rejected this offer.

Having considered the matter further I am persuaded Aviva's compensation offer of £4048.65 is fair and reasonable. I think it is possible that HMRC will refund some of the tax paid and it is not unreasonable that Mr R should apply to HMRC for this.

But having said that, I think Mr R will be put to considerable distress and inconvenience in having to liaise with HMRC. Given that he has had to work in each of five years that he otherwise would not have done, has been wrongly denied his annuity payments over that period and now has the added complication of reclaiming tax, I think his distress and inconvenience is considerable. I am not persuaded Aviva's offer of £700 for this is adequate. I think £1250 more accurately reflects Mr R's past and future distress and inconvenience.

my final decision

I uphold Mr R's complaint against Aviva Life Services UK Limited. It must pay Mr R £4048.65 as per its offer of 6 March 2018. It must also pay Mr R £1250 for distress and inconvenience. In total therefore it must pay Mr R £5298.65

Under the rules of the Financial Ombudsman Service, I am required to ask Mr R to accept or reject my decision before 16 April 2018.

Terry Connor
ombudsman