

The complaint

Mr N complains about his pension provided by Scottish Widows Limited (SW). He complained of poor communication and poor performance

What happened

Mr N said his complaint had various elements.

1. The way in which SW dealt with the provision of information in the months preceding 1 April 2022 as to the options he had for purchasing of an annuity and taking tax free cash (TFC). He had a very valuable Guaranteed Annuity Rate (GAR) worth around 9.8% but only available if taken on a specific date and to purchase an annuity with SW. He therefore wanted full information in advance to make an informed choice. He first made contact in December 2021 but did not receive a substantive reply so wrote again in January 2022 and was required to speak to a representative on the phone which was arranged for early March 2022. This was less than three weeks before the GAR vesting date. He was sent a quotation in March 2022. After taking the maximum TFC he should have been entitled to a GAR annuity or about £13,969. The March 2022 quote offered only around £13,600 which was about £350 less per annum. Mr N said that as it was less than 3 weeks from his GAR vesting date he felt he had no option but to accept the quote. He said SW's failure to provide information in a timely manner deprived him of the opportunity to make a considered decision.

2. SW required him to make a one-off final payment of around £3,537 (SFP) shortly before 1 April 2023. In error it asked for a net payment and then later a gross payment. It subsequently refunded the difference in July 2022. It did not explain why or what benefit he would receive by paying it. He was concerned that if he didn't pay he would lose the GAR. SW never referred to any policy conditions nor details of the benefits of the payment. SW said it was because he had only paid 29 years of premiums and needed to pay 30 years before the plan anniversary. He said the policy anniversary was in fact 28 September 2023 and not 28 March 2023. But as the policy was taken out on the basis of a retirement date of 1 April 2022 it was not clear why it didn't make the appropriate calculations at the outset to avoid this happening. Again he was not given information to make an informed decision.

3. His fund as at his retirement date, had grown by 6% over approximately 26 years. The median rate would have been 9% and the upper rate 12%. Even at the median rate this would have been a difference of approximately £100,000.

4. In 1999 he was told the GAR would not apply to new contributions so he did not make any additional payments into the fund and simply continued to pay in £300 per month. SW now said it didn't restrict contributions to the policy. He said had he known this he would have increased contributions to benefit from the GAR. Instead he put his money in a different policy which now had a value of around £350,000. In 2002 SW accepted the 1999 changes announced were not allowed in the light of a decision of the House of Lords. Since 2003 no bonuses had been paid. It seemed that SW were making decisions to mitigate the effect of the contractual requirement to pay a GAR and which negatively impacted the value of the policy. In effect the value of the guaranteed benefit had not increased from around £125,000

in 2002. He wanted to know how the final figure of around £189,000 was calculated and why the return over the life of the policy was only around 6% and what impact the GAR had on the decisions SW made in the light of the Equitable Life case about with profits funds.

5. He was sent an unrequested transfer value quote in March 2021 he felt this could be seen as an inducement to get him to transfer away and relieve SW of the GAR.

SW upheld Mr N's complaint. It apologised that it had not fully answered Mr N's questions and sent him £30. It accepted it did not send the correct quote to help him understand the SFP. It should have sent a quote showing the position without the SFP but in error sent one including it. It confirmed that had he not made the SFP his fund value would have been around £183,600 and he would have received tax free cash (TFC) of around £46,000 and an annuity of around £13,000. The SFP had increased the TFC by about £1,600 and the annuity by around £475 per annum. It confirmed that the amounts finally paid had been double checked and it confirmed that the amount was correct. It accepted it provided conflicting figures from the SFP. It refunded the amount overpaid for the SFP and paid interest of around £15 on that amount and £75 for distress and inconvenience. It apologised Mr N had to chase before it wrote to explain this.

SW later said the GAR was not dependent on payment of the final proportional premium (FP). The with profits (WP) benefits under this policy were calculated based on a premium term of 30 years (premium term is always calculated on full years). The entry date of the policy was 28 September 1993 and therefore the 30-year anniversary was 28 March 2023. At the selected retirement date of 1 April 2022 Mr N had paid 29 years' worth of premiums, and therefore, to receive the full WP benefits, he would have to make a Final Payment of around £353 gross (12 monthly premiums). The Final Payment was optional, and was not automatically collected.

My Provisional decision

I issued a provisional decision in this complaint and said the following.

Mr N raised several issues. I accepted that some of these were now broader than the original complaint that was made to SW. However this service had wide powers to investigate and as they were all related I thought it was reasonable to include them in this complaint. I was however required to make sure that SW has had an opportunity to comment on these. While I had raised them with SW I was issuing this provisional decision to make sure that both parties had fully understood what I had considered and my proposed conclusion.

1. Amount of annuity paid.

SW said that:-

- Tax free cash of £47,496.77 was paid on 04 April 2022 and an
- annuity of £13,594.32 is paid monthly in arrears and is guaranteed for 10 years, without increases or any dependants pension.

I believed that this was the accepted version of a quote sent to Mr N after his call with SW in March. The quote was based on a total fund of £124,718.01 and TFC of around £47,496.77 leaving £142,490.33 to purchase the annuity.

This compares to a GAR quote SW said it issued dated 1 February 2022 which had a:

- Total fund of around £189,000.
- Tax free cash of around £47,500
- Applying the balance to secure an annual annuity of around £13,969.

The notes to the quote Mr N accepted point out that the guaranteed annuity from 11 March 2022 was £13,969.75. This was clearly higher than the annuity which Mr N accepted. The notes point out that *'if you select our quote, you would be losing out on £375.43 per year'*. There are extensive further notes and warnings about the GAR and guide to GAR rates and suggestion that he takes financial advice.

It is clear that the annual annuity income accepted by Mr N was lower than the amount that he could have received had he taken the GAR annuity.

But I noted that Mr N's annuity carries a 10-year guarantee such that the annuity income would continue to be payable for the remainder of the 10 years in the event of his death within 10 years of its commencement. It is also paid monthly in arrears. These were valuable additional benefits as the GAR annuity did not carry any guarantee on death following its commencement and was paid yearly in arrears.

Mr N said he felt pressured into accepting the lower annuity and missed out. I had therefore considered the context at the time.

Mr N said he had been trying to get information from SW since December and was eventually told he had to have a call with SW which took place in early March 2022. By the time he received quotes following that call it was just under three weeks to his retirement date. He said he knew his GAR was only available at his retirement date and believed he had to accept before then. He didn't think there was enough time to get further quotes so decided to accept the one presented. When I asked him what he would have done differently if he had more time he says he would have accepted the GAR quote. He didn't think the addition of the 10-year guarantee and monthly payment was good value for the additional around £375 per annum he lost. These additional options were included in his quote because he asked for them. I said that because this is what the quote says.

Mr N said he made a choice without feeling he had all of the information. But I didn't agree. I thought the quote contained extensive warnings about the difference between it and the GAR rate. Given the extensive notes and warnings to the quote he must have been aware of the GAR, which was higher, but still decided to proceed.

Given the notes set out in detail how much the GAR would be, he was in a position to compare the two before accepting. Further SW said it had issued a GAR quote dated in February. So I thought that based on the evidence he was able to make an informed decision.

Further as he says there were still nearly 3 weeks left until his retirement date so time enough to ask questions but he didn't.

However I noted that SW said Mr N should have been made aware that an automatic 90-day extension period would be granted from his retirement date to allow him to make his decision. Mr N confirmed he was not made aware of this at the time. While I thought it would have been helpful to know this I still thought he had the information he needed to make an informed decision. But not having that additional time didn't prevent him making an informed choice, for the reasons already given. I had therefore considered an award for distress and inconvenience for failing to tell him about this at the time.

1. SFP

There is no dispute between the parties as to the amount of the SFP nor that SW requested a gross rather than net payment and eventually refunded the difference plus interest. SW confirmed that the rate of interest was 8% per annum simple which is the rate this service would have directed had it needed to do so. So I thought this payment was fair and reasonable.

I had however considered the explanation of the reasons for the payment, SW's power to request the payment and the impact it had on the benefits Mr N received.

SW said that Policy Provision 2.2.1 states that *"If recurring premiums are payable monthly a special final premium will be payable on the due date immediately prior to entry on pension on the original pension date"*.

I had reviewed the policy rules and could see that this section also goes on to say that

'The amount of the special premium will be equal to the monthly recurring premium multiplied by the number of months between that due date and immediately following anniversary of the date of entry.'

So it did seem that the policy terms permitted the additional payment. I note that SW requested 12 additional monthly contributions.

SW said the with profit benefits under the policy were calculated based on a policy term of 30 full years and the SFP was the total monthly premiums required from the retirement date (1 April 2022) to the next annual renewal date (28 March 2023). As this is a period of 12 months it seems that this also reflects the policy terms.

I had seen a copy of the original application form which shows a contribution of £100 per month which we know later increased to £300. It is signed and dated 25 March 1993.

SW said the entry date of the policy was 28 March 1993 so the anniversary of 28 March 2023 was correct. Mr N said this was factually incorrect. The policy commenced on 28 September 1993. 30 years from that date is 28 September 2023. Based on the original application form that I have seen on balance it seems to be that SW has used the correct start date.

It said the SFP was not linked to the GAR rate, but if not paid the fund to which the rate was applied would have been reduced accordingly. Mr N has not said he would prefer he had not paid the SFP and he seems to have benefited from it.

Given that SW had power under the policy terms to make the payment I didn't think it did anything wrong in requesting the payment.

However it requested too much but the excess was refunded with interest.

I do however think the communication surrounding this was poor and clearly conflicting requests were made so I had considered an award for distress and inconvenience. Mr N had not said that he would have opted not to make the payment, I thought the interest payment was reasonable and so I didn't think there was a financial loss.

Investment returns

Mr N was invested in a with profits policy. He complained about poor investment returns on over the around 30 years he had invested in it. Such funds are regulated by the financial regulator and in particular in its Conduct of Business Rules (COBS). These impose governance requirements and the need for a PPFM – a document that defines the Principle and Practices that the Society follows when managing with profits business.

SW said the total premiums since March 1996 were £96,560. It said the fund value of £189,987.10 at retirement was calculated as follows:

Guaranteed Cash Benefit: £112,900.00

Vested Bonus: £ 11,818.01

Terminal Bonus: £ 65,269.09

It confirmed that no bonuses have been paid since 2003.

It said the policy pay outs reflected the investment returns earned by the With Profits Fund over the lifetime of the policy.

It said the returns on the with profits fund reflected the market returns on the asset classes in which it invests; mainly shares, property and bonds issued by the government or by companies. Since 2000, several periods of difficult financial conditions had impacted on investment markets, most notably the bursting of the dot-com bubble in the early 2000s and the credit crunch of 2008.

It said the size of the regular bonus depended mainly on past investment performance, what guarantees it had already allocated to policies, and what it expected to happen in the future. The guarantees were comprised of the initial guaranteed minimum benefit and past regular bonuses. These guarantees anticipate investment returns and premiums due over the lifetime of policies. Since regular bonuses build up these guaranteed benefits for policies, if it were to do this too quickly, it would reduce the investment freedom for the With Profits Fund.

It would then have to invest more of the fund in lower-risk assets, such as cash or government bonds. Although lower risk, it expected these types of assets to provide lower returns over the longer run.

It would then expect to have less to pay out in total to policyholders. In its Principles and Practices of Financial Management (PPFM), it outlined that in some years there may be no regular bonus added to some or all with-profits policies that it managed. This was because it was committed to delivering the best long-term performance possible whilst also ensuring the Fund can meet its guarantees. To act in line with these principles, it withheld adding further regular bonus to policies like Mr N's from 2003.

Although it did not add any regular bonus to Mr N's policy from 2003 onwards, the annual returns earned were added to the with-profits fund for the benefit of its with-profits policyholders. This allowed a final bonus to be paid which was added when he retired. This was paid in addition to his policy's guaranteed benefits. The final bonus was set to ensure the total pension fund payable reflected Mr N's fair share of the with-profits fund. This included an amount to reflect the distribution of the Additional Account, which increased the return on Mr N's policy by 1.1% per annum from the date of demutualisation (3 March 2000). (The enhancement from the Additional Account is not reflected in the average investment returns listed.)

In addition to this, Mr N had a guaranteed annuity rate. This meant that he was able to use

his pension fund (which represented his fair share of the with-profits fund) to purchase an annuity on terms more favourable than those available on the open market. Note that the calculations of both the regular and final bonus rate did not take into account the guaranteed annuity rate available to a policy.

I thought the explanation provided by SW was reasonable.

I did understand Mr N's frustration that the policy has not performed as well as he might have wished. But I noted that SW did not provide Mr N with investment advice when he took out the policy and that a financial adviser was attached to the policy until around 2008. Mr N must have received benefits statements and it was open to him to take further financial advice if he was concerned about investment performance over the lifetime of his investment. As Mr N says there have been no bonuses added for many years so in his view the relatively poor performance is not a recent thing and he could have changed investments had he wished to do so, while weighing up the loss of the GAR.

I noted also that following letters in 1999 and thereafter regarding the guarantees attached to the policy he opted to place further additional contributions into a separate policy which he said was now worth around £350,000.

Mr N was not happy with the reply from SW and said there was no evidence or even any argument advanced as to how SW had conducted themselves consistent with the House of Lords decision in *Equitable Life Assurance v Hyman*. But that is a matter for the courts and not one that this service can comment on.

Mr N said the statements made by SW are at odds with the facts and are also contradictory to what is said in the literature to which they refer. By way of example he said the leaflet referred to statements that bonuses "*may be added at the end of each year*". This was wholly different to the practice which has prevailed for the past 20 years when no bonuses have been awarded in any year. The suggestion in SW's reply that no bonuses may be awarded in "*some years*" is at best misleading and is arguably being disingenuous. Mr N said the suggestion that if regular bonuses were awarded "too quickly" it would restrict investment decisions is almost laughable when the facts are that no bonuses have been awarded for 20 years and counting.

I noted his comments but the leaflet was clear that bonuses 'may be added' there was no commitment that they will be so I didn't think SW had failed in not adding bonuses and I found the rest of its explanation reasonable.

Mr N said it was noteworthy that SW had quoted average returns. He said it was telling that the levels of return prior to the *Equitable Life* case are significantly higher than the returns post that decision. It was also significant that this lower rate of return is compounded by the failure to award any bonuses since the *Equitable Life* decision and the level of returns produced by SW are significantly lower than the median rate for such funds.

Consequently, taken together he said the level of return and the failure to award any bonuses post 2003 have had a very significant effect on the value of funds which have the benefit of a GAR. SW have therefore imposed a double or even triple whammy on such policyholders. He said the effect of this is to reduce the cost of the GAR to SW.

While I noted his comments as I said he could have reviewed performance and taken further investment advice at any point had he wished to do so.

He said that no information was provided as to how decisions were made to make enhancements from the Additional Account, how the money in that account is amortised or

any actuarial advice upon which it is based and in the event there is a surplus in that fund, what happens to that fund? I had not addressed this further as I thought that SW had already provided a reasonable explanation regarding investment returns and I could not direct it how it applied the Additional Account.

Other issues

Mr N had raised a number of other issues. For completeness I had mentioned these below.

- He referred to a notice issued on 28 June 1999 to say that if he increased his regular contribution or added a one-off lump sum then the guarantee would not apply to the additional with profits benefit from 1 July 1999. Mr N said this accorded with his understanding but was different to the reply he received recently. In the light of that notice he said he opted to pay further increases of contributions into a new policy.

I had looked at the recent statement that SW did not limit contributions to the policy after 1999. He said had he known he might have made further contributions to his policy. But I thought this statement was consistent with the original statement. I said that because the 1999 statement didn't prevent further increases in contributions, it just made clear they would not benefit from the GAR.

- Mr N said SW sent a letter sent 12 months before his retirement date. He felt this was an enticement to miss out on his GAR. SW said this was a standard wake up letter, the purpose of which was to remind the customer of his pension benefits and his approaching retirement date. This seemed typical and reasonable to me.
- Mr N said there was some confusion in the record of total premiums paid to the policy as it did not initially show the SFP. This was however corrected and as explained above SW confirmed his benefits would have been reduced had the payment not been made.

Distress and inconvenience.

I considered an award for distress and inconvenience. Such an award was to reflect the impact on Mr N not to punish SW. It was clear that Mr N had to chase SW to get the information he needed. It was also clear SW didn't tell him he would have 90 days from his retirement date to make a decision on his GAR. Further he had to pay more than was needed for his SFP and struggled to get timely explanation as to why it was needed and the impact it would have on his benefits.

We all experience inconvenience in day-to-day life, but I thought these events and circumstances went further than that. I thought that a fair and reasonable award would be £600. To the extent that SW had already made payments for distress and inconvenience it need only pay the balance so that the total payment is £600.

I proposed to uphold this complaint in part and direct that Scottish Widows Limited should pay £600 for distress and inconvenience, to the extent that it had already made part payment it need only pay the balance to bring the total to £600.

SW commented that it had found a call from 1 March 2022 where Mr N was advised that he had a 90-day extension to make any decisions. On the call he questioned this and it was clarified again. I advised Mr N of this but he made no further comment.

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 have listened to the call that SW supplied and can see that he was notified of the 90-day period. I have therefore reconsidered my proposed award for distress and inconvenience in the light of that.

While I can see that he was advised of the 90-day period I remain of the view that overall he was put to inconvenience in chasing SW and he still paid more than the amount needed for the GAR. I say that because my provisional decision assumed he did not know about the 90-day period. But my assumption that he did not know was a matter of annoyance and I had already concluded did not prevent him making an informed decision. I therefore remain of the view that overall in the light of the level of distress and inconvenience caused an award of £600 is fair and reasonable in all the circumstances.

Putting things right

I remain of the view that my proposed award is fair and reasonable.

My final decision

I uphold this complaint in part and direct that Scottish Widows Limited should within 30 days of this service notifying it that Mr N has accepted my decision, pay £600 for distress and inconvenience, to the extent that it has already made part payment it need only pay the balance to bring the total to £600.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr N to accept or reject my decision before 7 January 2024.

Colette Bewley
Ombudsman