

**PENSION SCHEMES ACT 1993, PART X
DETERMINATION BY THE PENSIONS OMBUDSMAN**

Applicant	Mr Graham S Jones
Scheme	Lakeview Pension Plan No. 1
Respondent	Clerical Medical

Subject

Mr Jones complains that Clerical Medical, as administrator of his pension scheme, incorrectly calculated the tax free cash lump sum due to him, in consequence of which he was induced to transfer his benefits, and he suffered financial loss.

The Pensions Ombudsman's determination and short reasons

The complaint should be upheld against Clerical Medical. It is unlikely that Mr Jones would have acted differently had the lump sum been correctly calculated, but he should be compensated for his financial loss, as well as his distress and uncertainty.

DETAILED DETERMINATION

Material Facts

1. Mr Jones had a (defined contribution) occupational pension administered by Clerical Medical (**CM**). His employer made him redundant on 30 March 2001 and, in the light of uncertainty about the scheme being wound up, he decided to transfer his entitlement to a personal pension, Scottish Equitable's Phased Retirement Plan. This was on the advice of his financial adviser, TF, to whom, according to the formal letter of advice recording reasons, he had said that he disliked annuities, and would never purchase one. TF had been told by CM that the maximum lump sum available under the occupational scheme was £116,261.46, and the fund value was £586,202.55. He advised Mr Jones that the fund, plus enhanced allocation from Scottish Equitable, less bid/offer spread, would come to £623,719.51.
2. On 26 October 2001, TF sent CM details of his remuneration, by means of a document marked "SD" (ie, salary detail), prepared by Mr Jones, on the basis of which CM recalculated the maximum lump sum. TF and CM subsequently discussed the transfer terms and, after some misunderstanding about which Inland Revenue regime applied, the lump sum was eventually reconfirmed on 3 December 2001 at £116,261.46, based on final remuneration of £93,561, and the pre-1987 regime. CM has agreed it should have certified the maximum lump sum, to ensure Scottish Equitable knew the maximum death lump sum that could have been payable from the occupational scheme, but did not do so.
3. The CM policy was surrendered in December 2001, and the assets were transferred to Scottish Equitable in February 2002. In 2004 Mr Jones took his cash lump sum (£126,672), splitting the residue between income drawdown and an annuity; though he disliked annuities, he says he felt it was necessary then, because of his family and business circumstances. The occupational pension scheme subsequently wound up in 2006.
4. In 2009, Mr Jones complained to TF's firm about its fees. A response was given on 21 April 2010, in the light of which his new financial adviser, KT, advised him to query the lump sum calculation also. KT approached CM, and its senior customer service administrator carried out various calculations again. In the course of this, KT provided her with a breakdown payments made to Mr Jones in his final year, in the form of a letter from his employer dated 30 March 2001,

breaking down the figure for “Redundancy” in document “SD” into its component parts. KT said this showed a gross salary of £212,094.

5. Following further exchanges, on 22 December 2010 CM’s administrator emailed KT, saying that the final remuneration figure in 2001 should have been £145,478, and the lump sum £180,938. The final remuneration included an allowance for the taxable elements of his severance package, which were excluded from the 2001 calculation.
6. Mr Jones concluded that TF had permitted the lump sum to be miscalculated in 2001, and complained about this (and TF’s fees) to the Financial Ombudsman Service. On 31 May 2012, the Financial Ombudsman Service determined the complaint was not upheld, finding that TF was entitled to rely on the work of CM in calculating the final remuneration, which it found to be in error.
7. On 13 June 2012, Mr Jones decided to seek redress from CM. On 8 August 2012, CM said it could not establish how the figure of £93,561 had been calculated in 2001, but believed it may have taken final salary figure to be £90,561 and then added a (wrongly calculated) average of car allowances. CM also said it should not have recalculated the figures based on new information provided in 2010. Arguing that, despite the inaccuracies, Mr Jones had suffered no loss, it offered a small sum as redress for its poor service to him.

Document “SD”

8. Much of the dispute revolves around calculations based on document “SD”, which is headed “Salary Detail April 1995 to March 2001”. Its material figures are:

Tax Year	1997/98	1998/99	1999/2000	2000/01
Salary	72,266	79,162	87,078	90,561
Car Allowance	8,400	8,400	8,250	9,000
Profit Related Pay	437	1,570		
Bonus	16,012	5,937		
Stock Option Incentive		720	720	240
Buy out of Stock on CSC Take Over				3,268
Harmonisation of Terms and Conditions			53,539	

Redundancy				109,025
Unaccounted for	(88)	(788)	0	0
	97,027	95,001	149,587	212,094

Columns also provide figures for 1995/96 and 1996/97, but they have been omitted as not being material.

9. The document also includes explanatory notes on each of the items of remuneration listed (apart from Car Allowance). The ones which may be relevant are for Harmonisation of Terms and Conditions, and for Redundancy, for which the respective notes read:

“On relocating staff from London to Chertsey the Company harmonised the Terms and Conditions and the figure represents the buy out to harmonise my redundancy terms. If this had not happened the subsequent redundancy in March 2001 would have been increased by this amount plus any adjustment for subsequent salary increases.”

“Redundancy and payment in lieu of notice and holiday”.

Summary of Mr Jones’s position

10. Mr Jones believes that the potential lump sum figure of £180,938, calculated in 2010 by CM, was the correct one, and says that, if he had been given that figure in 2001, he would have taken the lump sum then, so that he could have invested it. He would have delayed drawing income from the Scottish Equitable Plan and would not have needed to buy an annuity when he did. He contends that he has suffered a financial loss, which he has said is difficult to quantify, though he has prepared some figures, based on the outcome of his alternative course of action, of taking his lump sum immediately.
11. He has also challenged the assertion that the 2010 recalculation was not based solely on document “SD”. However, he does not seem to mean that the original of that document was the only one used, but rather that the figures contained in it were adjusted when it became apparent that some detail had been excluded from it. The letter of 30 March 2001, made available to CM in 2010, itemised six components of the amount of £109,025, described as “Redundancy”. Two of these were statutory redundancy pay and company redundancy pay, while the others were pay in lieu of notice, car allowance for notice, compensation for loss

of benefits, and outstanding holiday pay. It is right that detail is taken into account.

Summary of Clerical Medical's position

12. CM has looked at the background and the calculations again, and argues that its administrator was wrong to have recalculated the potential lump sum, since she was using revised information which had not been available in 2001. (She had doubtless believed she was assisting Mr Jones with his claim against his adviser TF, not providing calculations which would be quoted against CM, her own company.) It has carried out further calculations, using the information in document "SD", and believes the final remuneration figure which should have been quoted in 2001 was £105,601, and the maximum lump sum £131,341.74.
13. It has acknowledged that, if that figure had been calculated at the time, Mr Jones would have received a larger lump sum, and so it is likely he has suffered some financial loss. However, it believes he would still have transferred his benefits to Scottish Equitable. As its original offer of compensation was solely in recognition of poor service, primarily through raising his expectations when providing inflated figures in 2010, and failing to certify the lump sum formally, it has increased its offer to reflect that possible loss.

Attempt at settlement

14. My office encouraged the parties to see if it was possible to reach a settlement. During these discussions, CM proposed that, if no settlement could be achieved, an independent expert be appointed to perform the correct calculation of the lump sum, based on the scheme rules and document "SD". It offered to make that appointment in August 2013, to which Mr Jones agreed, though with some reluctance. A suitable firm of experts was suggested in October 2013. However, it has not taken any such action.
15. Mr Jones has said that a third party will have to make a calculation based on document "SD", that he provided in 2001. As no independent expert has been appointed, I must determine the matter, by way of establishing the extent of Mr Jones' loss. While I have seen various accounts from CM of how final remuneration, and thus the cash lump sum, should be calculated, I cannot fully reconcile any of these with the figures on document "SD".

16. Currently, the settlement offer made by CM is £5,000. Mr Jones has calculated his financial loss as in excess of £75,000, but has indicated that he is prepared to negotiate a (presumably smaller) figure. The parties are clearly a long way apart, and my own calculations are not based on either of these figures, or other results quoted.
17. There are in essence three issues to determine in this case. First, what was the correct figure which should have been calculated as a cash lump sum? Next, what would Mr Jones have done if that figure had been known in 2001? Finally, to what extent has he suffered any financial loss as a result of these events?

Conclusions

Lump sum available

18. Over the years CM has made three different calculations. It now says the correct one is that carried out recently on the basis of the information available in 2001, which was the figures provided by Mr Jones in document “SD”, and he himself has said that the calculation will have to be made based on that document (though understandably he prefers the one made in 2010). Consequently, though there has been much debate about whether CM should have recalculated the lump sum in 2010, what information it should have used for that exercise, and whether (or to what extent) its conclusions can be relied on, I do not need to determine any of those issues. However, I do note that the extra information provided in the form of a letter dated 30 March 2001, breaking down the figure for “Redundancy” into its components, need not affect my calculation, since these components are all types of redundancy pay or payments in lieu, none of which would feature in final remuneration.
19. In carrying out the calculation, I bear in mind the relevant part of the definition of “final remuneration” in the Scheme rules:
- “... the highest remuneration for any one of the 5 years preceding the appropriate date being the aggregate of -
- (i) the basic pay for the year in question and
- (ii) the yearly average over 3 or more consecutive years ending with the expiry of the corresponding basic pay year, of any fluctuating emoluments

PROVIDED THAT fluctuating emoluments of a year other than the basic pay year may be increased in proportion to any increases in the Cost of Living Index from the last day of that year up to the last day of the basic pay year ...

PROVIDED THAT ... remuneration and total emoluments do not include any amounts which arise from the acquisition or disposal of shares ...”

This definition derives from the definition of the same term in the Inland Revenue Practice Notes IR12, subject only to minor differences which are not material. That definition states that:

“the total amount of any profit related pay (whether relieved from income tax or not) may be classed as pensionable remuneration and treated as a fluctuating emolument ...”

I also note that redundancy payments, whether statutory or otherwise, should not be included as emoluments in this calculation, as provided at the time under the definition of “remuneration” in section 612(1) of the Income and Corporation Taxes Act 1988, which refers to section 148 of that Act, which covers such payments.

20. On this basis, I find that, in 2000/01, the basic pay was £90,561, being the amount referred to as “Salary” in document “SD”. I consider the amounts under “Car Allowance”, “Profit Related Pay”, “Bonus” and “Harmonisation of Terms and Conditions” (but no others) to be fluctuating emoluments, and a three year average must be applied to them. They amounted to £8,400, £1,570, £5,937 and nil in 1998/99, to £8,250, nil, nil and £53,539 in 1999/2000, and £9,000 (and nil for the others) in 2000/01. That totals £86,696, and the three year average of those figures amounts to £28,899. Final remuneration was therefore £90,561 + £28,899 = £119,460 in 2000/01.
21. If a similar calculation were done for 1999/2000, the basic pay would be £87,078. The fluctuating emoluments amounted to £8,400, £437, £16,012 and nil in 1997/98, again to £8,400, £1,570, £5,937 and nil in 1998/99, and again to £8,250, nil, nil and £53,539 in 1999/2000. That totals £102,545, and the three year average of those figures amounts to £34,182. Final remuneration was therefore £87,078 + £34,182 = £121,260 in 1999/2000. As that is slightly more than the 2000/01 figure, that is the one which would apply.

22. CM has correctly said (and Mr Jones has not disputed) that, to calculate the cash lump sum, the final remuneration figure should be multiplied by 1.5 (the maximum lump sum at normal retirement date), and then reduced by the ratio of actual service (25.811 years) to potential service (31.1288 years), that is 82.917%. In this case, $£121,260 \times 1.5 \times 82.917\% = £150,817$.

What would have been done?

23. That lump sum is different from all of the three figures calculated by CM, but it is not as high as the second figure, which is the one on which Mr Jones, recognising it is the largest, wishes to rely. It is higher than the first amount calculated by CM in 2001, and I find that calculation to have been incorrectly carried out.
24. As the fund value in 2001 was £586,202.55, the potential cash lump sum from the personal pension, at 25% of the fund value, was then some £146,551, slightly less than the lump sum under the occupational scheme that I have calculated, but some £30,000 more than the sum that CM calculated at the time. Had Mr Jones been given a figure of £150,817 he would have expected it to change over time. In the event it seems to have decreased, as Mr Jones eventually took a smaller lump sum, though that is not the responsibility of CM. No doubt at the time the expectation would have been that it would increase.
25. Mr Jones says that, had he believed the potential lump sum in 2001 was £180,938, the figure calculated by CM in 2010, he would have taken that amount in 2001, instead of transferring his whole fund. We cannot know what he would have done, had he been told it was £150,817. He suggests he might still have taken the sum. However, it would only have been about £4,000 more than 25% of the total value with Scottish Equitable. Given that he did not need the cash at the time, and should reasonably have been expecting a better return from pension scheme investments than from cash outside the pension, I am not satisfied that Mr Jones would have taken the cash lump sum at the time.
26. Even if he would have done, the loss to him would have been relatively small, being the tax that drawdown income over time would have been subject to (the cash lump sum would have been tax free). In the event the cash that Mr Jones did take had reduced, through no fault of CM's, and was subject to a penalty, again not a direct consequence of CM miscalculating the cash in 2001.

27. He has, though, suffered a financial loss in one respect. With a cash sum certified at £150,817 in 2001, he could have taken a sum of about £164,802 in 2004, allowing for indexation at 3% pa (a figure submitted by Mr Jones, which I accept). In fact, he received £126,672, suffering a shortfall of £38,130. Though he has claimed that amount grossed up for tax, that is incorrect in my view, as he will (I must assume) get the benefit of the £38,130 in income, although he will pay income tax on it. I understand he was a basic rate taxpayer in 2004, so I assume that has remained the case since. The basic rate was 22% until 2007/08, and has been 20% since then. So over time he will pay, or will have paid, income tax of about £8,000, taking a rough average of those figures. He is entitled to redress for that.

Overall conclusion

28. I find that there was maladministration by CM, which has not at every stage been as helpful as it might. Mr Jones has suggested I should highlight this as a matter of conduct, but I do not consider CM's behaviour to have been so egregious that this needs particular mention. However, he has suffered financially, by way of additional income tax payable, and furthermore the fact that there was an error, and the difficulty of ascertaining what the correct figure should have been (including CM's own various attempts to recalculate it), have caused him significant inconvenience. Even now it is not possible to say with confidence what the wrong calculation was or what the figure should have been, and Mr Jones will always have that slight uncertainty.
29. For those reasons, I uphold the complaint against CM and make a significant award for distress and inconvenience, as well as redress for the financial loss.

Directions

30. Within 28 days of the date of this determination, CM is to pay Mr Jones £10,500, being £8,000 for his financial loss and £2,500 for the non-financial injustice he has suffered.

Tony King
Pensions Ombudsman

15 August 2014