

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

Applicant	Mrs Fiona Mary Bashford
Scheme	Scottish Widows Retirement Annuity Contract
Respondent	Scottish Widows plc

Subject

Mrs Bashford, as the legal personal representative of her late husband, has complained that she has not been properly compensated for the tax charges that arose on the death benefit payable in respect of her late husband's personal pension. Furthermore the tax charges had only arisen as a result of the procedures that Scottish Widows had followed in settling the payment.

The Pensions Ombudsman's determination and short reasons

The complaint should be partially upheld against Scottish Widows as they failed to adequately provide Mrs Bashford with information on the two year limit and the consequences of failing to return the documents within this two year timeframe.

DETAILED DETERMINATION

Material Facts

1. Mr Bashford had a Retirement Annuity Contract (**RAC**) with Scottish Widows. RACs are individual contracts between an individual and the pension provider. Under the terms of Scottish Widows' RAC in the event of the death of the policyholder the proceeds are payable on written notification of the death and receiving such proof as Scottish Widows may require to pay the benefits.
2. Scottish Widows were informed of the death of Mr Bashford by Mrs Bashford on 19 April 2005. The following day Scottish Widows advised Mrs Bashford that in order to settle the funds within her late husband's personal pension plan they would require the Death Certificate, a Grant of Representation, the Policy Schedule and a completed Claim form.
3. On 29 April 2005 Scottish Widows received the Death Certificate and Claim form from Mrs Bashford. They did not hear further until 2009, as described below.
4. The rules covering payment of death benefits changed with the introduction of new pension rules from 6 April 2006. Under the those rules, to avoid any tax charges a lump sum death benefit must be paid within two years of the earlier of the day the administrator knew of the member's death or the day the administrator could reasonably have known of the member's death. If the lump sum death benefit is not paid within two years of the earlier of these two days then it will be treated as an unauthorised payment and subject to tax charges. Transitional provisions were also introduced to protect members that had died before 6 April 2006 (known as "pipeline" cases) but again these required the lump sum death benefit to be paid within two years of the administrator being notified or when they could reasonably have known of the death. The transitional provisions did not apply in this case as the payment was made almost four years after Scottish Widows were notified of Mr Bashford's death and thus the lump sum death benefit was treated an unauthorised payment.
5. Scottish Widows sent Mrs Bashford three reminder letters for the documents still outstanding, the last of which was sent on 8 June 2007. The letters reminded Mrs Bashford that Scottish Widows needed the items requested in their letter of 20 April 2005 to proceed with the claim. No mention was made of any time limit or the possibility of a tax charge arising.

6. On 26 January 2009 Mrs Bashford called Scottish Widows to say that she would be sending in the remaining documents.
7. Scottish Widows received the final documents on 27 January 2009.
8. A pension scheme that makes an unauthorised payment will be liable for a scheme sanction charge. The charge is levied on the scheme administrator at a rate of 40% of the chargeable payment (or the aggregate of chargeable payments in a tax year). As the charge is intended to recover excess tax relief, it will be reduced by up to 25% if the member has paid an unauthorised payments charge.
9. On 2 February 2009 Scottish Widows made a payment of the policy proceeds under the policy amounting to £40,218.11. This payment was net of an HMRC unauthorised payment tax charge of 40%, because the payment was being made more than two years after the death of the policyholder.
10. On 31 March April 2009 Mrs Bashford's solicitors, Hart Brown, contacted Scottish Widows and queried why the unauthorised payment tax charge had been levied. They said:

“The rules that applied prior to April 2006 seem to suggest that if payment of the policy proceeds cannot take place within 2 years of a member's death (or notice of the death) the policy proceeds are to be held on bare trust for the executors absolutely. If this is the case the funds are held outside the pension scheme arrangement and hence no unauthorised payment/tax charges would be applied when the policy proceeds are paid out.”

11. On 17 April 2009 Scottish Widows replied that the post-April 2006 rules applied as the death benefit was not paid within two years of when they could reasonably have known of Mr Bashford's death.
12. On 16 December 2009 Hart Brown made a formal complaint to Scottish Widows on behalf of Mrs Bashford. They referred to exceptions for “pipeline” cases where entitlement arose prior to April 2006 as in Mr Bashford's claim. Hart Brown also said:

“It is evident that in your capacity as scheme administrator you have made no attempt to comply with very clear 'pipeline case' guidance which if followed would have avoided the unauthorised tax charge payment. This is despite the fact that your Legal Department was clearly aware of the importance of making payment prior to the two year rule as stated in your letter of 17 April 2009.

It seems to us that you were under a clear duty of care, initially to the policyholder and after the death then to the person(s) entitled to the

fund, whoever they might transpire to be. Under that duty you were beholden to consider what your options were under the rules, and to take whatever lawful steps were open to you to maximise the benefit available under the policy.

...

With this mind we are seeking compensation for Mrs Bashford in respect of the scheme sanction charge (£26,812.07) and the unauthorised payment charge and the unauthorised payment surcharge (both yet to be quantified) and interest on these sums from the dates their loss was suffered by our client until reimbursement by you.

Please note that no legal costs are being sought at present, but that if our client is not satisfied with your response to this complaint the matter will be referred to the Insurance Ombudsman and if necessary court proceedings will be issued - in which event interest and costs will be claimed.”

13. Scottish Widows investigated the complaint and in their letter of 18 August 2010 to Hart Brown said they accepted an "element of liability." They also said:

“However we are in principle accepting that we should have done more to inform Mrs Bashford of the rule changes regarding taxable pension benefits and that in not doing so we are liable for the majority of the additional charge levied against the final sum.”
14. In a further exchange of emails over the claim Hart Brown confirmed that the total claim amounted to £68,148.67 and to this interest on the 40% scheme sanction charge already deducted would have to be added.
15. Scottish Widows acknowledged the email and agreed that the tax position should be confirmed and paid before they made any compensation. Mrs Bashford therefore engaged an accountant to help with the completion of the self-assessment tax return. Scottish Widows did make enquiries as to how this was progressing in June and July 2011.
16. Hart Brown say there was a delay in paying the unauthorised payment tax charge was because the accountant on whom Mrs Bashford depended failed to do his job properly and subsequently “disappeared” leaving her to instruct another accountant, who had not previously been involved in the matter.

17. On 22 March 2012 Hart Brown confirmed that the tax had been paid and enclosed a HMRC screen print to show that this amounted to £42,731.89 made up as follows:

Tax	£36,866.59
Late Payment Surcharges	£ 3,686.64
Interest on late payment	£ 2,178.66

18. Hart Brown also enclosed with their letter a string of emails with Mrs Bashford's present accountant which confirmed that the surcharges were for two late payment charges of 5% (as the payment had not been made by 31 January of the year following the end of the tax year in which the charge arose) and interest on the tax. The email also said that HMRC had a year to decide whether to charge penalties for the late return.
19. Hart Brown therefore asked for the £26,812.07 deducted in February 2009 to be paid. They also said "that leaves Mrs Bashford out of pocket – we say inappropriately and on account of the failings of Scottish Widows – as shown on the screen print."
20. After a further exchange of emails Scottish Widows replied on 21 July 2012 and enclosed a cheque for £34,945.01 representing the return of the original amount held back of £26,812.07 plus an interest payment of £8,132.94 (at 8% a year compound). Scottish Widows also said:
- "I can see that the original complaint handler (name of person) wrote to you on 18 August 2012 confirming that we were accepting an 'element of liability'. ...we agreed (internally) that we would accept 50% liability for the tax costs."
21. On 5 September 2012 Hart Brown sent Scottish Widows a copy of a statement of account from HMRC confirming that a tax payment of £36,866.59 had been paid together with surcharges of £3,686.64 and interest of £2,178.66. The letter was acknowledged by Scottish Widows on 6 October 2012.
22. On 18 October 2012 Hart Brown wrote to Scottish Widows and asked if Scottish Widows would confirm that they would pay:
- the sum of £36,866. 59 plus interest at 8% from the date of payment to date of receipt
 - £5,865.30 (representing the surcharges and interest paid on £36,866.59) plus interest at 8% from date of payment to date of payment
 - Hart Brown's costs

23. Scottish Widows replied on 17 December 2012 and outlined their position. They referred to the information they requested when first notified of Mr Bashford's death and said:

“We required the Death Certificate, Grant of Representation, the Policy Schedule and completion and return of our Claim Form.

We can only value a policy on receipt of formal notification of death by receiving the original Death Certificate. This is our standard requirement when settling pension and life cover policies. We also requested Grant of Representation due to the value of the policy. Our procedure is to request sight of a Grant of Probate when the total value of all claims is greater than £50,000.00. This ensures that the proceeds of a claim are paid to the correct party.”

24. They also said they had agreed to consider payment for the majority of the potential tax charge which they listed as:

Scheme Sanction Charge @ 15%	£10,054.53
Unauthorised payment charge @ 40%	£26,812.07
Unauthorised payment surcharge@ 15%	£10,054.53
Total	£46,921.13

25. Scottish Widows also asked for documentary evidence of the final tax charge payable as a direct result of the death benefit being an unauthorised payment. They also said that they could not agree to pay the £5,865.30 cost of the surcharges and late interest payments imposed by HMRC or interest on this amount as this was not as a result of an error on their part but resulted from an issue with Mrs Bashford's accountant. In addition Scottish Widows said that as a general rule they did not cover the costs if a customer raised a complaint through a third party. They did however agree to consider this further if Hart Brown would provide a breakdown of the costs.
26. On 26 February 2013 Hart Brown provided documentary evidence of the final tax charge payable and repeated their assertion that the tax charge would not have arisen if the payment had been made within two years or transferred to a separate account outside of the scheme. They also said that they did not accept that the delays were attributable to anyone other than Scottish Widows.
27. On 6 March 2013 Scottish Widows replied and said:
- “Firstly, I must reiterate that it was not possible under the rules of this policy to move the funds to an account outside of pension tax rules. This is something that is only possible where we hold the policies under a Master Trust and we have the authority to make payments at our discretion. These trusts only existed for pension policies taken out with us after 31 July 1988. This policy was taken before this time and

consequently was not held under a Master Trust but was a direct contract between Scottish Widows and Mr Bashford. We therefore had no authority to move the funds to protect them from any tax charge.

In respect of the late fees, it was not as a result of any error on our part that the tax charge was only paid to HM Revenue & Customs (HMRC) in early 2012. The claim value and interest (less 40%) were paid out in February 2009. We have always been clear that the tax charge was correct and agreed to cover a proportion of this as early as 2010. This was only paid by in 2012. Therefore we do not consider that any delays in actually paying the tax charge to HMRC can be attributable to Scottish Widows. We will not be covering any late fees charged by HMRC.”

28. Scottish Widows also commented on Hart Brown’s claim for reimbursement of legal fees and said

“I consider that at least 8 letters/emails to us would not have been necessary had we reacted appropriately to your correspondence. Based on the fee schedule you have provided and allowing for the customer contact you indicated it appears that approximately £400.00 of the charges made to Mrs Bashford would not have necessary. We are therefore prepared to make a payment for that amount towards the solicitor fees.”

Summary of Hart Brown’s position

29. Scottish Widows were in a special position to know about the “two year cliff” and should have notified Mrs Bashford of it but did not do so. They should also have considered whether given the dramatic effect of the two year cliff being passed it was essential to insist on their own rules being honoured to the letter. If necessary they should have waived or adapted them to enable the statutory requirement to be complied with.
30. Scottish Widows could also have made a special arrangement to effect a payment that would have meant that the two year cliff would not be relevant.
31. There was no formal guidance as to how insurance companies deal with a death claim for retirement annuity contracts. They were given very considerable latitude by HMRC who could be described as almost being keen to help the two year cliff to be avoided. It would have been possible to organise a transfer of the funds to an account in the names of temporary trustees prior to the expiry of the two years if Scottish Widows been suitably proactive. That account would have been controlled by Scottish Widows so Scottish Widows could have been sure that when the personal representatives produced the grant of probate to them they would be in a position to meet their obligation to the estate.

32. Hart Brown accepts that it would only be in exceptional circumstances that legal costs are awarded. The costs sought are those arising out of correspondence with Scottish Widows – making the complaint, pressing it despite their delays, prevarications and arguments only capable of being mounted once a detailed grasp of the unusual and complex regulations had been mastered. If Scottish Widows had dealt with the complaint efficiently and co-operatively the costs would have been minimal and would not be being sought, but the contrary was the case. It was the way in which they dealt (or failed to deal) with the complaint that fully justifies those costs being awarded.

Summary of Scottish Widows' position

33. Scottish Widows say they never agreed to accept full liability in this case as they could not commit to paying any amount without having the full facts and figures.
34. Scottish Widows admit that it is possible that they could have submitted further reminder letters and that they did not confirm the change in legislation to Mrs Bashford when this occurred (April 2006). However there is nothing to suggest that this would have resulted in a settlement of the benefits prior to 19 April 2007. It is questionable whether any further action by Scottish Widows would have made a difference to the date that the final documentation was received. Scottish Widows did set out its required documentation almost 4 years before the documentation was received and no explanation has been given for the length of time taken to provide this.
35. It was not possible for Scottish Widows to move the funds to protect against an unauthorised tax charge being applied after two years of non-settlement. This would only have been possible if the policy had been held under a Master Trust and Scottish Widows had the authority to make payments at its discretion. Master trusts only existed for pension policies taken out after 31 July 1988. Mr Bashford's policy was taken out before July 1988 and was a direct contract between Scottish Widows and Mr Bashford. Scottish Widows therefore had no authority to move the funds to protect them from any tax charge.
36. Scottish Widows does not agree with Hart Brown's view that in accepting that more could have been done in this case then Scottish Widows is 100% liable for the tax charge. It is not a simple case of Scottish Widows either accepting full responsibility or no responsibility at all. It is entirely possible, and indeed fair and reasonable where it is the case, to accept only an element of responsibility.

37. Scottish Widows does not accept that if Mrs Bashford had been contacted earlier the tax charge would not have applied or that they are responsible for Mrs Bashford's delay in settling the tax charge with HMRC. It is for this reason that Scottish Widows has decided not to cover the tax charge in full, provide 8% interest for the entire period that monies were held, or cover all associated costs. Scottish Widows have now paid the majority of the tax charge and consider this a fair resolution.

Conclusions

38. First, I find that the transitional provisions for pipeline cases did not apply in this case as the payment was made almost four years after Scottish Widows were notified of Mr Bashford's death and thus the lump sum death benefit was treated an unauthorised payment. I also find that under the terms of the RAC it would not have been possible to move the money to a separate arrangement to avoid the unauthorised payment tax charge as Hart Brown have suggested.
39. Scottish Widows have said that no explanation was given as to why it took almost four years to receive the final documentation including the grant of probate. My office has also asked for information as to why it took so long to obtain the grant of probate. We have been told that it was primarily caused by delay in obtaining details of the value of Mr Bashford's property and business interests from his accountants. Hart Brown say that Mrs Bashford agreed to make herself responsible for chasing the accountants in order to minimise her legal costs.
40. Scottish Widows were aware of the two year limit but did not make Mrs Bashford aware of it. They have said that even if they had made Mrs Bashford aware of the two year limit there is nothing to suggest that this would have led to an earlier settlement.
41. In my judgment Scottish Widows should have made Mrs Bashford aware, as they now accept. Mrs Bashford was responsible for obtaining the information necessary to enable the grant of probate to be obtained from the accountants. It is perhaps surprising that she did not place greater pressure on them, but as far as she was concerned all that was at risk was lost interest or growth on the death benefit during the period of delay. If she had been advised of the significant financial consequences of failing to provide the information within the two year limit then I consider it more likely than not that she would have ensured that it was provided.
42. The main consequence of Scottish Widows failure to provide the relevant information was that Mrs Bashford became liable for the unapproved payment charge

of £26,812.07 and the unauthorised payment surcharge of £10,054.53. There was also a Scheme Sanction Charge of £10,054.53 which Scottish Widows agreed to meet.

43. The unapproved payment charge of £26,812.07 and the unauthorised payment surcharge of £10,054.53 arose directly from Scottish Widows failure to provide sufficient information on the two year limit and so I find that Mrs Bashford should be fully reimbursed for these amounts.
44. Mrs Bashford's liability to pay the unauthorised payment tax charge arose in February 2009, when the proceeds of the personal pension policy were paid to her. Payment of the unauthorised payment tax charge was due by 31 January 2010 but it was not made until January 2012 and so Mrs Bashford also had to pay late payment surcharges of £3,686.64 and interest for late payment of £2,178.66. Mrs Bashford is also seeking recovery of these costs.
45. The delay was caused by the accountant Mrs Bashford first instructed. Scottish Widows have said that they are not responsible for it. Hart Brown say the interest would not have arisen if Scottish Widows had settled the benefit within the two year limit and therefore they should also be liable for this amount.
46. I find that Scottish Widows are not liable. The matter was entirely outside their control, as they say.
47. Hart Brown have also asked for interest at the rate of 8% to be paid on both the unauthorised payment tax charge of £36,866.59 and the late payment surcharges of £5,865.30 from the date of payment to date of receipt. I agree that Scottish Widows should pay interest on the unauthorised payment tax charge of £36,866.59 for the period that this sum was not available to Mrs Bashford i.e. between 20 January 2012, the date of payment recorded on the HMRC statement and date of receipt but only in line with the base rate for the time being quoted by the reference banks. As I have found that Scottish Widows are not responsible for the late payment surcharges it follows that Scottish Widows should not be liable for any interest charge on these amounts.
48. Hart Brown have also asked for their remaining fees to be paid due to the need to understand the unusual and complex regulations involved with this complaint. (Scottish Widows have already reimbursed Mrs Bashford £400 of Hart Brown's fees because of delays in responding to their enquiries.) I do not normally award legal costs unless I also consider the matter a complex one. In my view this is a relatively

straightforward matter. It was Mrs Bashford's decision to instruct a solicitor. I therefore make no order in respect of Mrs Bashford's legal fees.

49. I do however consider that this whole issue would have caused Mrs Bashford some distress and inconvenience and I think she should be compensated for this.

Directions

50. I direct that within 28 days of this determination Scottish Widows are to make the following payments to Mrs Bashford.
- £36,866.59 plus simple interest in line with the base rate for the time being quoted by the reference banks between 20 January 2012 and date of payment, less any amounts already paid to her in respect of the unapproved payment and unapproved payment surcharge. Scottish Widows are also to provide Mrs Bashford with a reconciliation of the amounts paid to date.
 - £200 as compensation for the distress and inconvenience that she has suffered.

Tony King
Pensions Ombudsman

26 January 2015