DRN-3880471

Financial Ombudsman Service

The complaint

Mr O complains that The Prudential Assurance Company Limited has unfairly deducted a Market Value Reduction ("MVR") from the value of his pension savings when he asked that they be transferred to another provider. He says that Prudential failed to make him aware that his pension plan had been amended such that a MVR could be applied. And he says that Prudential changed his normal retirement age ("NRA") without his agreement, so denying him the opportunity to take his pension benefits without a MVR being applied.

What happened

I issued a provisional decision on this complaint in December 2022. In that decision I explained why I didn't think the complaint should be upheld. Both parties have received a copy of the provisional decision but, for completeness and so those findings form part of this decision, I include some extracts from it below. In my decision I said;

> *Mr O held pension savings with Prudential. Those pension savings had arisen as a result of additional voluntary contributions ("AVCs") that Mr O made in addition to pension benefits he accrued in an occupational pension scheme. Prudential managed the AVC scheme on behalf of the occupational scheme. Mr O first started to make his AVC payments more than thirty years ago.*
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> *In 2011, Mr O entered a phased retirement agreement with his employer. At that time he told Prudential that he wanted to cease making contributions to his AVC plan, but wished to retain the scheme. And he told Prudential that he didn't want to take his AVC benefits at that time. It appears that Prudential recorded Mr O's wishes as being an indefinite deferment of his retirement date. Mr O took his pension benefits from the main occupational scheme in 2013 when he'd reached 65 years of age. But he didn't take his AVC benefits at that time.*
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> *In October 2020 Mr O asked Prudential to transfer his AVC pension savings to another provider. At that time Prudential confirmed to Mr O that it would be applying a MVR to the value of his pension savings. Mr O complained to Prudential about the MVR that had been applied.*
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> *When Prudential looked into Mr O's complaint it identified that a target retirement date ("TRD") of 27 March 2012 had been applied to his policy. Whilst it noted that a TRD has no financial impact on the policy it had been unable to identify when, or why, that TRD had been added. So it paid Mr O £125 for the inconvenience he'd been caused. But Prudential said that the implementation of a MVR had been fair and its calculations had been correctly carried out.*
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> *The AVC policy that Mr O held was taken out more than 30 years ago. So it is unsurprising that, over the intervening years, some of the relevant documentation has become lost. I don't draw any adverse conclusions from that missing documentation – generally businesses aren't required to keep correspondence and other documents indefinitely. But it does present me with some difficulties when seeking a definitive answer to some of the matters that Mr O has raised.*

I think it would be first helpful to share my understanding about the various components of the AVC policy that underpins Mr O's complaint. His AVC policy was operated by Prudential on behalf of his occupational pension scheme. And ultimately, since Mr O was a teacher, changes to the AVC scheme would need to be agreed by the Secretary of State for Education. Once he had taken the AVC policy Mr O was then able to choose how to invest his contributions. He chose to place his contributions in Prudential's With Profits fund. But the documentation from the time also suggests other investment options such as a range of unit linked funds, or the use of a Deposit fund that was described as operating in a similar manner to a building society account.

With profits funds are a type of 'pooled investment' fund. Consumers pay into the fund along with a number of other investors and their money, along with that of the other members, is put together and invested in stocks, shares, equities, bonds and property over a set period of time. This diversity, and the ability to change the proportions invested in each of these types of investment, helps to balance the level of risk and the expected increases in the fund value in the long run.

What distinguishes with profits funds from other pooled funds is 'smoothing'. Smoothing aims to reduce the direct impact of market changes on the fund investments and means that investors are less directly exposed to rises and falls in the value of their investments over the shorter-term. This is of great benefit especially where a with profits fund is being used to fund something which happens at a specific date such as retirement.

But over time it became clear that consumers taking some or all of their benefits from the fund at other times might result in them receiving an unfair share of the underlying assets. So, for smoothing to work, there needs to be a mechanism to protect the whole fund from being depleted by investors trying to exit after for example a market fall. This protection is the MVR about which Mr O is complaining. They are generally intended as a short-term measure that will be removed once the business feels that its funds have recovered sufficiently. But sometimes they will continue to be applied for extended periods.

MVRs were relatively rare before 2001 so I think it unlikely that it would have been something that Mr O was aware of when he first agreed to pay into the AVC policy. I don't know when Prudential first made consumers aware that MVRs might be applicable to their pension savings. And Prudential hasn't been able to locate any specific correspondence about its introduction. But Prudential has provided a copy of a letter it sent to Mr O in 2008 that made reference to the possibility of a MVR being applied in the future. And it seems that the regular annual statements Mr O has received from Prudential since around that time also contained similar information.

In 2011 Mr O was required to complete a form for Prudential when he asked to defer taking his AVC benefits. Although I will consider that form in a little more detail later in this decision, it does also provide information about a MVR being applicable to Mr O's AVC savings – although at that time the MVR was quoted as being nil.

So although I'm not able to determine exactly when, or how, Mr O was first made aware that a MVR might be applied to his policy, I'm satisfied that he would have been aware, by around 2011 at the latest that there was a possibility of a MVR being applied in the future. And, although in 2011 the MVR was shown as being nil, Mr O took no steps to move his AVC investments into an alternative fund. So my

conclusion must reasonably be that the future possibility of a MVR being applied didn't make the with-profits fund unattractive to Mr O.

As I said earlier, Mr O has pointed out that changes to the AVC scheme required the consent of the Secretary of State for Education. But I don't think the introduction of the MVR falls with the scope of that definition of a change. The AVC scheme remained the same, and consumers were able to place their AVC savings into the with-profits fund, or the other available investments. What had changed were the terms of one of the investment funds. I don't think changes such as that should be considered to be a change to the scheme as a whole.

In line with many funds of this nature, Prudential didn't apply a MVR at two distinct events. The MVR wasn't applicable if AVC benefits were taken, or transferred, at the normal scheme retirement age of 65. And it wasn't applicable if the benefits were being taken, or transferred, following the death of the member. So it might have been possible for Mr O to have taken his pension benefits in 2013, when he reached the normal scheme retirement age, without the application of the MVR.

When Mr O took phased retirement in 2011, it doesn't seem that was something that Prudential would normally expect to deal with. Mr O has said that it was a relatively unusual approach, and that in fact his own employer stopped making any further offers of that nature after his phased retirement had been agreed. So I wouldn't be surprised that Prudential didn't have a defined process, or paperwork, to handle Mr O's situation.

In 2011 Mr O wanted to stop contributing to his AVC, but retain the benefits. It seems that request, combined with the notification it had received of Mr O's phased retirement, set Prudential off down a path of dealing with a member's full retirement. So Mr O was asked to complete a benefits claim form. Mr O returned that form indicating that he wished to defer buying his pension. I entirely accept that the nature of the form meant there was no other relevant option that he could choose. But by ticking that option, it seems Prudential replaced Mr O's normal retirement age of 65 with the maximum for the scheme, that being 75 years.

So by making that change, Prudential didn't send to Mr O the paperwork that would normally be issued in the lead up to retirement. So it is possible that Mr O would have been unaware, or certainly not reminded, that reaching the normal retirement age of 65 gave him the opportunity to take his AVC benefits without a MVR being applied. But I'm not persuaded that has caused any detriment to Mr O.

Firstly I don't know, and Prudential is unable to tell us, whether a MVR would have generally applied in April 2013 when Mr O reached age 65. As I said earlier Prudential wasn't applying a MVR when Mr O deferred his benefits in October 2011. But I accept, if by then a MVR was applicable, taking the benefits at age 65, free of a MVR might have been attractive.

But, as I've already explained, I think Mr O should have been aware that a MVR could be applied. And he took no steps to change his AVC investments in 2011 when he was told they were free of any MVR. Mr O took his pension benefits from his main occupational scheme in 2013, but didn't take those from the AVC plan, or even enquire about taking the benefits from the AVC plan, at that time. So I'm not persuaded that, taking his AVC benefits at that time, even if they were free of a MVR, would have been something that Mr O would have chosen even if he'd received the appropriate reminder pack.

I appreciate that what I've decided here will be disappointing for Mr O. But I think it is important to remember that a MVR doesn't arbitrarily reduce the value of someone's pension benefits. Instead it ensures that the withdrawal from the fund fairly reflect the underlying value of that consumer's share of the fund assets. Other consumers in the with-profits fund will have suffered MVRs when taking their benefits in the past. And the effect of those MVRs will have been to protect the value of Mr O's AVC savings that remained in the fund at that time.

So on balance I don't currently think this complaint should be upheld. Whilst I cannot determine when, or how, Mr O was made aware of the introduction of the MVR by Prudential, I think it likely that the matter would have been explained to him. And Mr O's later actions, when the MVR was explained in letters and annual statements, lead me to conclude that he wouldn't have taken the decision to alter his investments even if I thought the communication of the change had been deficient. I don't think Prudential's failure to communicate with Mr O in the lead up to his 65th birthday caused him any detriment.

I invited both parties to provide us with any further comments or evidence in response to my provisional decision. Prudential has said that it has nothing more to add. Mr O doesn't agree with my provisional decision and has provided some extensive additional comments. Although I am only summarising here what he has said, I want to reassure Mr O that I have read, and carefully considered, his entire response.

Mr O has reiterated that he still considers the introduction of the MVR to be a substantial change to the contractual terms of the AVC scheme. So he thinks that the change did require the approval of the Secretary of State. He has asked whether any evidence has been provided either showing that consultation took place, or that Prudential received legal or regulatory advice stating that no consultation was needed.

Mr O points out that "smoothing" of with-profits funds operated well before MVRs were introduced. He says that any risk was effectively managed by the use of Terminal Bonusses. He is concerned that there is insufficient transparency and independent audit of Prudential's historical bonus decisions. He feels that effectively Prudential is "judge and jury" without any meaningful accountability for its decisions.

Mr O says that, given the significant nature of the change introducing a MVR, Prudential should have sought his express consent for the change. If that consent had not been provided he thinks it would have been reasonable for Prudential to terminate his contract until such time that consent was provided.

Mr O accepts that when he first took out the AVC policy the normal retirement age was set at 65 years. But he notes that subsequent changes to legislation meant that employment contracts could no longer require retirement at that age. So he says any normal retirement age in the terms of his AVC plan should no longer have applied. He says that when he stopped his contributions in 2011 he reasonably concluded that he could determine his own target retirement date. He says the only reference to an end date that he was aware of was that his plan needed to end by age 75.

Mr O says that his decision to cease making contributions in 2011 was not due to his phased retirement, although he accepts that both decisions occurred around the same time. He says that he wanted to retain the plan as he had no need of the additional income at that time and was hopeful that his investments would continue to grow and that annuity rates might improve. He says that at that time, although the small print of the communications from Prudential did refer to MVRs, he thought (wrongly) that their use would be unlikely in the next few years.

Mr O says that Prudential's lack of evidence of him being told about the introduction of the MVR is most likely because no communication took place. He says that he was unaware how the MVR would be operated, and specifically that it wouldn't be applied at the normal scheme retirement age of 65. He says that when he became aware of the change he did consider moving his pension savings to another provider, but concluded that there would be little benefit in doing so. He says that had he thought about or been made aware of the matter earlier, he might have considered the purchase of added years benefits to be more suitable. But by 2011, and even some years earlier given his age, Mr O says the OPS would have told him that it was too late to make a change of that nature.

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.

As in my provisional decision, in deciding this complaint I've taken into account the law, any relevant regulatory rules and good industry practice at the time. I have also carefully considered all the submissions that have been made by Mr O and by Prudential, including those in response to my provisional findings. Where the evidence is unclear, or there are conflicts, I have made my decision based on the balance of probabilities. In other words I have looked at what evidence we do have, and the surrounding circumstances, to help me decide what I think is more likely to, or should, have happened.

I've thought carefully about the additional comments provided by Mr O in response to my provisional decision. I would like to thank him for the care and diligence he has shown in presenting his additional arguments. But I am sorry to tell him that those additional comments haven't persuaded me that I should change my findings on his complaint. I would however like to take this opportunity to further discuss some of the matters that he has raised.

As Mr O will be aware I am required by the legislation to decide complaints on the basis of what I think is fair and reasonable. So, although I will take account of the law, I am not bound by legislation. This service provides an informal alternative to the Courts, and so some of my findings might lack the depth of evidence that Mr O has suggested needs to be present. Where evidence is unavailable, for whatever reason, I will use my judgement to decide what I think is most likely to have happened.

I remain satisfied that the changes to the with-profits investment option did not constitute a change to the AVC scheme in general, such that would require the consent of the Secretary of State. As I explained in my provisional decision that investment was one of a number of options available to members paying AVCs. So I don't think it necessary to explore further whether consent was sought for that change.

The management of with-profits investment funds is closely regulated and requires the publication of performance and investment data by fund managers on a regular basis. But the calculation of bonus amounts, or MVRs, is largely at the discretion of the investment firm. Those calculations need to balance the rights of investors to receive a fair return on their capital, together with the need to ensure the ongoing sustainability of the fund. Those aren't matters that fall within the remit of my consideration of this complaint – should Mr O hold concerns over the way Prudential is operating the fund he should raise the matter with the regulator – the Financial Conduct Authority.

As Mr O quite rightly points out, the absence of any evidence from Prudential showing its communication of the introduction of the MVR could lead to a conclusion that no announcement took place. But I still consider that possibility to be unlikely. I don't share Mr O's suspicion that Prudential took a commercial decision to introduce the change and hope that a lack of transparency, and the natural lack of inertia for change, would lead to policyholders remaining with the firm.

Mr O has said that, around 2011, he was aware of the possibility of a MVR being applied and that he considered other options for his pension savings. At that time he concluded he had little to gain from moving to another provider – who I think would most likely also have applied similar MVR policies. I cannot therefore reasonably conclude that, even if Prudential had failed to communicate with Mr O when the MVR was first applied, better information would have led to a different approach from Mr O.

In his introduction to his additional comments Mr O briefly touched on what happened when he was first sold the AVC plan. He has expressed concerns that he might have been better making added years contributions rather than taking the AVC plan. But as Mr O notes he has no evidence to support a claim that the AVC plan was mis-sold to him. And without him having made a complaint to Prudential about what happened when he first started the AVC plan, I cannot reasonably make any conclusions about the initial sale in this decision.

Mr O has said that his phased retirement agreement had no specified end date. So, at that time, he had no clear indication about when he would actually retire and take his pension benefits. So I don't think it was unreasonable for Prudential to take his request as an indefinite deferral of his retirement date, and set his normal retirement age to 75 – the maximum allowed by the scheme. As I've explained, that change didn't prevent Mr O from taking his benefits earlier, or alter his benefits in any way. It was simply Prudential's working estimate at that time of when Mr O might retire.

Making that change did have the impact of Mr O not being sent the normal documentation as he approached age 65. But as I previously explained, that would most likely have told him that he could take his benefits without the application of a MVR – but not because of that being a specified time within the rules of the scheme, but more because MVRs were not generally being applied at that time. As Mr O has said himself, in 2011, his expectation (albeit that he accepts it was incorrect) was that MVRs would be unlikely to be applied in the next few years. I don't think that view would have been different in 2013 when he might have received the scheme information as he turned 65 years of age.

I understand how disappointing my decision will be for Mr O. But my findings, as set out in my provisional decision remain unchanged. Whilst I cannot determine when, or how, Mr O was made aware of the introduction of the MVR by Prudential, I think it likely that the matter would have been explained to him. And Mr O's later actions, when the MVR was explained in letters and annual statements, lead me to conclude that he wouldn't have taken the decision to alter his investments even if I thought the communication of the change had been deficient. I don't think Prudential's failure to communicate with Mr O in the lead up to his 65th birthday caused him any detriment.

My final decision

For the reasons given above, and in my provisional decision, I don’t uphold the complaint or make any award against The Prudential Assurance Company Limited.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mr O to accept or reject my decision before 21 March 2023.

Paul Reilly
Ombudsman