

The complaint

Mr and Mrs P's complaint is about the maturity value of a mortgage endowment policy they had with Phoenix Life Limited. They were paid less than they were expecting and think that Phoenix didn't pay them the correct amount. As a result, Mr and Mrs P have said they now have a significant credit card debt which they arranged to cover the shortfall, and have suffered a lot of anxiety and stress.

What happened

Mr and Mrs P took out their mortgage endowment policy in July 1998 when they were members of staff at the original product provider. It was a traditional with-profits policy, providing life cover of £43,000 and it had a basic sum assured of £22,120, to which bonuses would hopefully be added during and at the end of the term. The monthly premium was £93.60 and they've told us that they paid a higher premium than normal to ensure a better financial return at maturity.

The annual statement sent to Mr and Mrs P on 31 December 2022 detailed the value of the policy with the addition of that year's bonus as £32,84.91. This was made up of the basic sum assured and already added bonuses. The surrender value, which included an element of terminal bonus, was detailed as £60,899, which was not guaranteed.

Phoenix sent Mr and Mrs P a letter on 17 May 2023 reminding them that their policy was due to mature shortly. It explained what they needed to do and provide to receive the maturity value. On 31 May 2023 Phoenix wrote to them again and told them that the estimated maturity value was £56,790.29. Mr and Mrs P raised concerns about this figure, as it was lower than they were expecting.

An annual policy update was sent to Mr and Mrs P on 7 June 2023. This confirmed that the policy was on track to reach its target value of £43,000. It detailed maturity values using assumed growth rates, which projected that the policy would be worth between £60,600 and £65,400. It was explained that the rate of growth needed to achieve the target value was less than the middle rate used, but then went on to say that it might be appropriate for more conservative assumptions to be used if the policy was in the last five years of its term. It was also confirmed that it was impossible to be certain about future investment growth and the maturity value could be lower or higher than shown in the illustrations, particularly if the policy was due to mature soon.

On 20 June 2023 Mr and Mrs P were provided with a surrender value for the policy. It detailed that the basic sum assured and bonuses already attached, totalling £32,084.91, was guaranteed to be paid at maturity. At that time a terminal bonus of £36,255.94 was detailed along with the statement '*This amount might be payable in addition to the sum assured and existing annual bonuses at maturity or on earlier death. The payment of a final bonus is not guaranteed and the value is reviewed regularly.*' The estimated maturity value that '*could*' be paid was detailed as £68,340.85. It was detailed that this sum was not guaranteed and could be higher or lower than that amount.

Mr and Mrs P were paid a maturity value of £56,790.29. They complained as the value was significantly lower than they had been led to believe it was and they thought it was wrong.

Phoenix responded to the complaint on 31 July 2023. It said that the maturity value it paid Mr and Mrs P was correct. It explained that the surrender value they'd been given on 20 June 2023 had been calculated using the incorrect terminal bonus rate – that for a policy with a term of 24 years, rather than one of 25 years. Phoenix also confirmed that on 1 July 2023 the terminal bonus rates were reduced to reflect the then recent downturn in the performance of the with-profits fund. Phoenix considered that it should have explained this to Mr and Mrs P earlier and offered them £100 compensation for any trouble or upset the delay had caused them. It offered £10 to cover the cost of the calls they made to it.

Mr and Mrs P were unhappy with Phoenix's response and referred their complaint to this Service.

Phoenix confirmed that the terminal bonus rates that applied to Mr and Mrs P's policy were reviewed as normal on 1 January 2023 and 1 July 2023. On both occasions the rate was reduced. It also confirmed that the 20 June 2023 figure provided to Mr and Mrs P had been calculated incorrectly assuming a term of 24 years, rather than a term of 25 years. The terminal bonus rate for the shorter term was higher, which meant that the terminal bonus used in the calculation was 28% higher than it should have been. Following the reduction in terminal bonus rates as of 1 July 2023, the terminal bonus rate for a 25-year policy dropped by a further 8%.

One of our Investigators considered the complaint, but he didn't recommend that it be upheld. He was satisfied that the amount Mr and Mrs P had received was the amount they were entitled to, and the reason the maturity value was lower than expected was due to an error in the 20 June 2023 figure and the terminal bonus rate being reduced shortly before the maturity date. The Investigator was satisfied the compensation payment and reimbursement for telephone calls, was fair in the circumstances.

Mr and Mrs P didn't accept the Investigator's conclusions. They asked that the complaint be referred to an Ombudsman and set out a number of 'inconsistencies' that they wanted addressed and for phoenix to prove that it had paid the correct amount. Mr P explained that he had worked for the original product provider for over ten years and understood how endowment policies work. During the time he worked for the original product provider they had taken out three endowment policies, two of which were to act as repayment vehicles for interest-only mortgages. The first of those policies had matured in 2014 with a very significant shortfall of over £24,000, which they accepted because their annual statements had predicted this.

The policy subject to this complaint was the second of those policies, and they had paid a higher premium for the policy to increase the amount of money invested. As such, they expected to receive much more than the target value attached to the policy. When they had moved again, because the policy had been projecting a maturity value of over £60,000 for several years, they didn't take out an additional repayment vehicle for the £20,000 increase in borrowing, assuming the surplus projected would cover the increase. So Mr and Mrs P consider the fact that the policy in question exceeded the target value is irrelevant.

Mr and Mrs P said that Phoenix had come up with an implausible explanation to cover up the fact that it had not paid out the correct amount. They said their complaint was that they believed Phoenix was dishonest and hadn't paid them the correct amount.

The Investigator considered everything Mr and Mrs P had said, and responded to their points, but he was not persuaded to change his conclusions about the complaint. As agreement couldn't be reached, the complaint was passed to me for review.

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.

The policy subject to this complaint is a traditional with-profits mortgage endowment. That meant there was a contract under which Phoenix had to pay a basic sum assured (in this case £22,120) plus any accrued bonuses when it matured. While Mr and Mrs P may have been given projections about the potential future performance, these aren't the same as providing a legally binding guarantee.

I think it would be useful to explain how the addition of bonuses affect the maturity value of this type of policy. This policy can attract two types of bonus - annual bonuses and a terminal bonus. Once annual bonuses are added they are guaranteed but the terminal bonus isn't guaranteed until it is paid. Each year Phoenix would take into account such issues as the bonuses already declared, any benefits that have to be paid under policies, previous investment returns and what returns may be possible in future before deciding the level of the annual bonus to be applied.

When annual bonuses are decided upon, a process called 'smoothing' is used. This means that in some years some of the growth within the fund is reserved to support the fund in years where returns are poor or negative. This means that when a policy matures or is surrendered before that date, the amount payable as the basic sum assured and annual bonuses, may not be a true reflection of the policy's share of the fund. In order to make up any shortfall in the value of the fund that has been assigned to a particular policy, a terminal bonus will be added. It is calculated as a percentage of the total of the basic sum assured and annual bonuses (adjusted for early surrender).

As Phoenix has explained, it is normal for it to review the terminal bonus that applies to such policies twice a year and the reviews are applied as of 1 January and 1 July each year. While those are the standard review dates, if unexpected events cause uncertainty within the financial markets, additional reviews can be done. Most product providers did additional reviews in recent years in response to the Covid-19 pandemic and the Russian invasion of Ukraine. Based on the evidence Mr and Mrs P have provided, it would appear that Phoenix did an additional review that was applied in August 2022.

Mr and Mrs P have questioned how Phoenix could know what the new terminal bonus rates would be when it produced the maturity value at the beginning of June 2023 if the review was not completed until 1 July 2023. The date of the review is the date it is applied to Phoenix's systems and takes effect on policies. Calculating a terminal bonus is a complex matter and so will take place before the 'review date' to enable the new rate to be applied on that date. So the new rate will be known at a high level for a short period before it is applied, hence Phoenix being able to give Mr and Mrs P an accurate figure for their maturity value slightly before the maturity date. However, the bonus rate would not be applied across the board to Phoenix's systems in general until the review date.

As Phoenix said in its final response letter, it is unfortunate that Mr and Mrs P weren't told earlier why the maturity value they were provided with at the beginning of June 2023 was lower than other information they could access.

Phoenix has confirmed that the terminal bonus rate that should have been used in the 20 June 2023 calculation was 85%, but it incorrectly used a rate of 113%. When the terminal bonus rates then dropped on 1 July 2023, the rate was reduced to 77%. That change in bonus rate does account for the difference between the maturity value and the figure provided in the 20 June 2023 letter. I note that Mr and Mrs P don't believe Phoenix that a mistake was made, and they believe it has made up an excuse in order to pay them less than they are entitled to. I can understand why Mr and Mrs P are unhappy that the value they received from the policy was less than they thought it would be, but I have seen no evidence that Phoenix calculated the maturity value incorrectly or did something to deny them money they were entitled to.

When Mr and Mrs P entered into the contract for the endowment policy they agreed to pay Phoenix a premium each month. Phoenix had to invest the premium, taking costs as and when required from the fund. As far as I can see that is exactly what it did. Growth over the policy term has turned the premiums paid into a maturity value which unfortunately was less than Mr and Mrs P hoped for and was adversely affected by events and performance close to the maturity date. However, I am satisfied that Mr and Mrs P were paid what they were entitled to when the policy matured.

Phoenix offered Mr and Mrs P £100 for the upset and inconvenience they experienced because it was slow to explain why their maturity value was lower than they'd expected. I have considered this and I think it a fair and proportionate amount in the circumstances. In addition, the £10 Phoenix has offered to cover any telephony costs Mr and Mrs P incurred, seems reasonable, given they haven't indicated it is not sufficient to cover their costs.

My final decision

Phoenix Life Limited has already made an offer to pay Mr and Mrs P £110 to settle the complaint and I am satisfied this offer is fair in all the circumstances. As such, my final decision is that Phoenix Life Limited should pay £110 in full and final settlement of this complaint.

Under the rules of the Financial Ombudsman Service, I am required to ask Mr and Mrs P to accept or reject my decision before 16 August 2024.

Derry Baxter

Ombudsman