

## complaint

Mr A's complaint against The Prudential Assurance Company Limited ("Prudential") relates to the amount of bonuses and the investment performance of his personal pension which is invested in Prudential's with-profits fund. He is disappointed with the declared bonuses over the last ten years and is unhappy that they do not appear to reflect the underlying performance of the with-profits fund.

## background

Mr A's pension was originally invested with another provider who was taken over by Prudential in 2001. Mr A's funds are invested in Prudential's with-profits fund. Mr A is concerned that the level of bonuses paid since Prudential took over the fund in 2001 have fallen. The underperformance of his fund over a ten year period is at a time when Prudential has said that its with-profits fund has grown by over 100%.

The complaint was investigated by one of our adjudicators. He set out the background to this complaint and his findings in December 2013.

The adjudicator did not recommend that the complaint should be upheld. In summary, he said that the level of bonuses declared by Prudential was not guaranteed. He provided Mr A with a copy of Prudential's *Principles and Practices of Financial Management* ("PPFM") and explained that this set out the basis on which Prudential is required to manage its with-profits fund.

The adjudicator also explained that Prudential, in common with other with-profits fund managers, used a process called 'smoothing'; this essentially means that with-profits fund managers hold back returns achieved in years of good investment returns in order to counterbalance bad years. This means that the level of bonuses declared in any one year will not necessarily reflect the investment performance of the underlying assets in the with-profits fund over the same period.

In addition, the adjudicator explained that the declaration of bonuses was a matter for the Prudential in exercising its legitimate commercial judgement and was therefore beyond the remit of this service to investigate.

Mr A did not agree with the adjudicator's conclusions. He said, in summary, that:

- He had received a copy of the PPFM but still had seen no evidence that he had been treated fairly.
- The allocation of bonuses since Prudential took over management had not reflected the performance of the market.
- Prudential's with-profits fund has grown by 100% since 2003 (one year 8.8%, five year 20.1% and ten year 111.1%) yet his plan has reduced compared to the contributions he has made.
- The actual returns on his policy had been negative in that the "*fund value at the commencement of the 10 year period was £33,161.413 and the latest statement was £35,580.48...*" after he had net premium of nearly £3,200.

- He wanted to know if Prudential had distributed profits fairly, if at all and whether there would be a terminal bonus that would make up the growth over the period. He said without transparency he was left with the impression that the investment was losing money every year while the underlying fund grew every year.
- He asked the adjudicator what evidence he had obtained to make his decision as he did not accept that his decision was based on the PPFM document alone.

## my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

Having carefully considered the points Mr A has made regarding the fairness of Prudential's bonus allocation policy I agree with the conclusions of the adjudicator and for the same reasons.

The industry regulator, (previously the Financial Services Authority ('FSA') and now the Financial Conduct Authority ('FCA')) recognise that the managers of with-profits funds have significant discretion about how they operate their with-profits funds. Notwithstanding that, the regulator's Principle 6 requires that firms "...*must pay due regard to the interests of its customers and treat them fairly*". Furthermore, the Conduct of Business Sourcebook provides specific rules and guidance for fund managers on the operation of their with-profits funds including:

*"With-profits business, by virtue of its nature and the extent of discretion applied by firms in its operation, involves numerous potential conflicts of interest that might give rise to the unfair treatment of policyholders" and "A firm must have good reason to believe that its pay-outs on individual with-profits policies are fair."*

Prudential is therefore accountable to the regulator for the way in which it operates its with-profits funds; it must ensure that it does so in accordance with its Principles and Practices of Financial Management document and all other relevant regulatory obligations.

The regulator monitors the management of with-profits funds in a number of ways. These include a requirement on with-profits fund managers to appoint a with-profits actuary for whom the regulator provides rules and guidance on their duties and responsibilities. There is also a requirement to appoint an independent with-profits committee whose remit is to protect the interests of the with-profits policyholders and ensure that they are treated fairly.

I note that Mr A feels that the bonuses he has received does not reflect the underlying performance of the with-profits fund. However Mr A's plan is a traditional with-profits plan and as Prudential said in their response to Mr A's complaint, when the plan was taken out it guaranteed a certain level of retirement fund between ages 60 and 75. The guaranteed funds already allowed for an element of growth; the fund value could potentially be increased by the addition of annual bonuses and a terminal bonus.

Therefore the current guaranteed fund figure of £35,580.48 at age 65 is not the same as the current fund value, or its value on retirement; it is calculated on the basis that contributions continue to this age and already allows for an element of growth. If contributions were to cease then Prudential would reduce the guaranteed benefit and potentially any terminal bonuses that might be payable. On the other hand, if investment performance allows, then

the addition of annual bonuses and a terminal bonus could significantly increase the fund value at retirement.

I note Mr A's concern about the lack of transparency as to how bonuses are allocated and that he feels the bonuses credited to his policy are not in line with the underlying performance of the fund. However, it is not within the remit of this service to carry out an in depth audit of Prudential's management and operation of its with-profits fund - as explained above, it is the regulator that monitors the management of with-profits funds. Matters of this nature may be reported to the FCA if consumers consider that they have not been treated fairly.

However, having approached the FCA to ascertain if there are any concerns about the way in which Prudential is operating its with-profits fund, I can confirm that no such concerns were expressed.

The amount of bonus paid each year, if any, is determined by Prudential's investment objective, consistent with its regulatory obligations, to allocate bonus amounts as fairly as possible to all its investors in its with-profits fund with the aim of providing a competitive return at the end of the term.

Bonus rates take into account various factors; these include not just current or recent investment performance but also how Prudential expect the fund to perform in the future, as well as the fund's liabilities in respect of the guaranteed benefits applicable to all plans.

As explained by the adjudicator it is normal for with-profits fund managers to employ 'smoothing' in determining the level of bonuses it pays. This means that it does not pass on all the returns received on the funds in good years so that it can pay a bonus when returns are not so good. Such a process is fundamental to the way with-profit funds operate; details of the process are documented in the PPFM.

I appreciate Mr A's disappointment at the decreasing level of bonuses that have been paid in the last ten years. However, for the reasons set out above, it would be neither fair or reasonable to conclude that he has been treated unfairly by Prudential.

### **my final decision**

I do not uphold Mr A's complaint against The Prudential Assurance Company Limited.

Terry Connor  
**ombudsman**