DRN-4189357

The complaint

Mrs L complains that the Non-Protected Rights (NPR) part of her Personal Pension (PP) plan held with Zurich Assurance Ltd (Zurich) unfairly lapsed without a value. This was in stark contrast to the performance on the PR part of her PP.

What happened

Mrs L has a PP that she originally took out with a business that has since become part of Zurich. She started the PP on 1 April 1989. The plan comprised NPR benefits and former Protected Rights benefits. And was used to contract out of the State Second Pension (S2P), formerly known as the State Earnings Related Pension Scheme (SERPS).

Mrs L's application form for the PP shows that she chose to invest as follows:

MANAGED 50%, EQUITY 30%, PROPERTY 20%.

Mrs L made personal contributions into the plan between 1989 and 1991, with the last payment made on 1 July 1991. The total personal contributions made was £539.28, with £179.92 of basic rate tax relief. The overall total was £719.

A total of £2,496.81 PR contributions were also made on behalf of Mrs L in for the tax years from 1987 through to 1990. A total of five separate payments were received by the plan between 1 September 1989 and 1 September 1991.

Zurich said it wrote to Mrs L in 2012 to confirm that from 6 April 2012 the Government had removed the choice to contract out from S2P, so no further former PR payments were expected.

Mrs L said she decided to review all of her pensions in 2021. She said that when she contacted Zurich about the value of her PP, she discovered that the NPR part of her PP had lapsed without value in December 2010. But the PR part was valued at £31,221.62 in January 2022.

Mrs L asked Zurich to explain the situation. She was unhappy that the NPR had lapsed without value. She felt that if the NPR funds had been invested in the same way as the PR funds, they would've had a value of around £8,890.

Mrs L also asked Zurich to provide annual statements from February 2000 to February 2011, so that she could see what had happened to her NPR. But Zurich told her it didn't hold historic copies of the annual statements she'd requested.

Mrs L complained to Zurich in November 2022 about the NPR benefits in her PP. She said that a 20 January 2022 letter from Zurich showed that she'd paid a total of £719 of personal contributions into her plan. And a further letter had shown the value of these as of 11 February 2000 was £643.78. Mrs L wanted to know why her NPR funds hadn't been invested in the same way as her PR funds. She also felt that the charges Zurich had applied had been unreasonably high, and out of proportion to the investment amount.

Mrs L felt that Zurich should correct the position of her NPR fund to what she felt they would've been worth now, had they been invested in the same funds as her PR funds. She also felt it should compensate her for the inconvenience and stress caused by her complaint.

Zurich issued its final response to the complaint on 7 December 2022. It didn't think it had done anything wrong. It said it'd invested Mrs L's funds in line with her application for the PP. And it'd administered her PP in line with its terms and conditions. Zurich also said that the charges and the lack of contributions, as well as the volatility of the stock market, had led to the NPR lapsing without value. It also said that it hadn't been able to let Mrs L know about this at the time as it didn't hold an address for her at that point.

Mrs L wasn't happy with Zurich's response. So she brought her complaint to this service.

Our investigator didn't think the complaint should be upheld. He said he'd seen no evidence that Zurich had applied the charges incorrectly. Or that the plan had been invested incorrectly.

Mrs L didn't think our investigator had fully addressed the crux of her complaint, which was why her NPR contributions hadn't been invested in the same way, with the same charges, as the PR contributions. She said Zurich had acknowledged that Capital units grew at a lesser rate than Accumulation units. And that the charges for the Capital units were higher than those for Accumulation units.

Mrs L also said that Zurich had told her that when she reached her selected retirement age of 50, it would've converted the Capital units to Accumulation units. But this was already too late for her to benefit from, as the value of her NPR had already lapsed to zero before then. She felt this had been due to the excessive charges of the Capital units relative to those of the Accumulation units: 3.5% plus an Annual Management Charge (AMC) of 0.75% for the Capital units compared with an effective annual charge of zero for the Accumulation units.

Mrs L queried whether her application form showed that she'd actively selected Capital units rather than Accumulation units for her NPR. She asked why she would've done so. And felt that all of the contributions into her PP, both NPR and PR, should've been invested in the better growth rate Accumulation units. Had this happened, she would've now been better off. So she felt that Zurich should correct the value of her NPR to what it would've been if it'd been invested in the same Accumulation units as those for her PR.

Our investigator shared a copy of the terms and conditions of the PP with Mrs L, which he said he felt would've been shared with her at the plan's inception. He referred her to the section covering Capital and Accumulations units and the section which covered Unit Allocations. While he acknowledged that the terms and conditions was a long and detailed document, he said it had been Mrs L's duty to read before she had started her plan. And that she could've raised any issues she'd had with the charges at the time.

Our investigator also shared with Mrs L a copy of the application form she'd completed, noting that it didn't cover Capital and Accumulation units. But he said it did confirm that Mrs L had wanted to have 50% of her funds in the Managed Fund, 20% in the Property Fund and 30% in the Equity Fund. He said he couldn't see any evidence that Zurich had invested the funds outside what Mrs L had requested.

Mrs L didn't think there was anything in either the terms and conditions, or the application form, which stated that her NPR contributions would be invested in Capital units. She confirmed that neither the choice of funds, nor their performance, was the issue here. Instead, she said it was the fact that Zurich had decided to invest all her NPR contributions into Capital units, with higher charges and lower growth, whilst the PR were all invested in

Accumulation units with lower charges and higher growth.

As agreement couldn't be reached, the complaint has come to me for a 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.

Having done so, I'm not going to uphold it. I can see that Mrs L feels very strongly about her complaint, so I know my decision will be disappointing. I'll explain the reasons for it.

I should perhaps first explain the Financial Ombudsman Service is not a regulatory body.

The Financial Conduct Authority regulates financial services firms and financial markets in the UK. But what I'm considering here is whether Zurich has acted fairly and reasonably in the way it applied charges to Mrs L's plan.

I first want to give a brief background to the charging structure being used for Mrs L's plan.

The charging structure

In some older plans like this one, any regular contributions in early years were often used to buy or Capital units. These were sometimes called Initial units. These had a higher annual charge than Accumulation units, which were bought with the contributions later on.

The reason for this was that the provider had usually paid an initial commission or salary to the adviser. This assumed that the consumer would pay into their plan for the whole term up to retirement, whether they actually did so or not. So the provider recouped most of the costs from the premiums paid into the plan in the early years.

If a consumer didn't continue to contribute to the plan for very long, a bigger proportion of the plan would be made up of Capital units, compared to the situation if the contributions had continued in full to the consumer's retirement date. Capital units attracted a higher annual charge as a percentage of the units invested. So this meant that the average charge per unit was higher if contributions ended early.

The smaller the pension value, the higher proportion of the plan was taken up in charges. So it's not uncommon to see plans lapse without any value altogether before the consumer reaches retirement.

Stopping or significantly reducing contributions part of the way through the policy also meant the consumer could be paying higher overall charges for the policy than set out in the illustration they were given by the adviser, because this would've assumed contributions continued up to retirement.

I next considered the specifics of what happened to Mrs L.

Mrs L's specific situation

I understand that Mrs L only made personal contributions into her PP for a little over two years.

The plan's policy provisions state that NPR contributions made during the first two years will be used to purchase Capital units, rather than Accumulation units. As noted above, these units were subject to higher charges than the Accumulation units which would've been purchased after two years if Mrs L had still been making contributions.

Because Mrs L’s NPR fund was composed of predominantly Capital units, given when her contributions stopped, the charges reduced its growth, eventually leading to its value lapsing to zero.

Zurich said that the plan has been administered in line with the plan terms and conditions. And that a copy of these would have been sent to Mrs L at the time the policy started.

Zurich further stated that in the first two years, the plan only purchased Capital units and those units incurred a 3.5% charge throughout. It also said that these units incurred the whole of the AMC and grew at a lesser rate than the Accumulation units. It said that as a Mrs L’s NPR fund was mostly held in Capital units, the charges were higher than if payments had continued. If they had, Accumulation units would’ve been purchased.

Zurich also said that the PR element of Mrs L’s plan only ever purchased Accumulation units as there weren’t any setting up charges for this part.

I’ve carefully considered the terms and conditions of the plan. They confirmed that in the first two years Zurich correctly purchased Capital units with the NPR contributions. These incurred a 3.5% charge throughout the term of the plan. The Capital units also incurred the whole of the AMC and grew at a lesser rate that the Accumulation units.

The terms and conditions also confirmed the AMC is reinvested into the plan to buy additional units; so it isn’t a charge to the plan.

The Capital units remain in place and incur the additional 3.5% Capital unit charge from inception until the selected retirement age. At the selected retirement age, the Capital units are converted to Accumulation units. Unfortunately, due to the NPR contributions only continuing for a little over two years, Mrs L’s NPR fund had lapsed to zero before she reached her selected retirement age.

I acknowledge that Mrs L considers she’s been treated unfairly, as she believes that her NPR contributions should’ve been invested in Capital units from the start of her plan. But I can’t fairly agree.

I say this because the plan terms and conditions stated that Accumulation units would only start to be purchased after two years for the NPR contributions. And as Mrs L didn’t contribute for much longer than two years, she would’ve only built up a small proportion of Accumulation units with her NPR contributions. The plan charges had to be paid for in some way. And they wouldn’t have been covered if all of Mrs L’s NPR contributions were invested in Accumulation units from the start. Therefore I can’t reasonably say that Zurich has treated Mrs L unfairly. Or that it has failed to follow the terms and conditions of her plan.

I acknowledge that Mrs L doesn’t consider it fair that the PR part of her plan and the NPR part of her plan have been treated so differently. But I’m satisfied that both were correctly administered under the terms and conditions of the plan.

Therefore I can’t fairly say that Zurich has done anything wrong. And I don’t uphold the complaint.

My final decision

For the reasons I’ve given above, I don’t uphold the complaint.

Under the rules of the Financial Ombudsman Service, I’m required to ask Mrs L to accept or reject my decision before 31 July 2023.

Jo Occleshaw
Ombudsman