HEAD OFFICE
Johannesburg
3rd Floor, Digital House
Cnr 5th Street & Park Lane
Sandton, 2196
PO Box 651826, Benmore, 2010
Tel (011) 884-8454 Fax (011) 884-1144
E-Mail: enquiries-jhb@pfa.org.za

Cape Town
2nd Floor, Oakdale House, The Oval
Oakdale Road, Newlands, 7700
P O Box 23005, Claremont, 7735
Tel (021) 674-0209 Fax (021) 674-0185
E-mail: enquiries@pfa.org.za
Website: www.pfa.org.za

Re: DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT, 24 OF 1956 ("the Act") – AL BROPHY v CENTRAL RETIREMENT ANNUITY FUND & SANLAM LIFE INSURANCE LIMITED

Introduction

[1] Having considered the complaint received by this office on 15 March 2005, I consider it unnecessary to hold a hearing in this matter. My determination and reasons therefor appear below.

Facts

[2] You became a member of the Central Retirement Annuity Fund ("the fund") with effect from 1 April 2002. The fund is administered by Sanlam Life Insurance Limited ("Sanlam Life") which also invests its assets. At the inception of your membership Sanlam Life issued a policy of insurance to the fund on your life. Your chosen date of retirement was 1 April 2026. Your initial contribution was R2 000.00 per month which was to increase automatically every year by 10%. Your assets in the fund were invested in Sanlam Life's International Equity Fund. Having received notification that you did not have tax clearance you ceased, with effect from 1 May 2003, your contributions to the fund. At that stage you had made contributions to the fund for 13 months in the amount of R26 200.00. According to the fund, by 1 May 2003 your policy had lapsed and it had no paid-up value. I can only assume that the insurer's expenses equaled or exceeded your fund value. The insurer has not provided a specific breakdown of its expenses.

The complaint

[3] You are essentially dissatisfied with the charging of the "premium

termination fee", which effectively wiped out your entire contributions. You are of the view that it is excessive and unfair as you aver that the rules of the fund make no provision for such deductions. You are further aggrieved that Sanlam Life failed to inform you that you stood to forfeit all your contributions if you failed to obtain a tax clearance certificate. You aver that Sanlam Life failed to advise you that a tax clearance certificate was compulsory for purposes of this policy. You also complain that the respondents refused your request to switch your funds to another policy held with the fund, namely the Balanced Fund (SA). You lastly complain that you were not allowed to temporarily halt or reduce your contributions, which you argue falls foul of the rules of the fund.

The responses

[4] The fund has raised a technical point that the complaint pertains to the policy of insurance between the fund and the insurer, Sanlam Life, and as such constitutes 'long-term insurance business' over which I do not have jurisdiction.

[5] The fund also contends that the complaint does not fall within the definition of a "complaint" in section 1 of the Act and for this reason too I am precluded from investigating and determining the matter.

[6] On the merits, it is argued that you were warned of the consequences of prematurely ceasing your contributions. The fund relies on rule 2.4 of part 6 of the rules which reads:

> "2. Membership of the FUND will be terminated if
> …
> 2.4 a MEMBER ceases to make further contributions before the POLICY (*sic*) assuring the MEMBER's benefits obtains a paid-up value, unless the FUND owns another POLICY on the MEMBER's life."

Reliance is further placed on rule 2 of part 7, the apposite portions of which read:

> "2. A MEMBER's CONTRIBUTIONS are payable during the period determined in the POLICY issued on his life.
>
> If a MEMBER'S CONTRIBUTIONS cease after he has already paid sufficient CONTRIBUTIONS so that the POLICY issued on his life has a paid-up value in accordance with the practice of the ASSURER, the ASSURER converts the POLICY to a paid-up POLICY for reduced benefits."

[7] Reliance is further placed on clauses of the policy document as justification for the charging of a "premium termination fee" and the "lapsing" of the policy. The clauses, which are contained on page 8 of the

document read:

> **"Can payment of recurring premiums (if applicable) be stopped?**
>
> Yes. If the sum to which the value of the policy investment has grown, less a premium termination fee, exceeds the minimum of the foreign currency equivalent of R1 500.00, the policy will be maintained without further premium payments. This minimum will increase from time to time.
>
> If payment of recurring premiums is stopped before the option date, this premium termination fee currently consists of the following:
>
> - the foreign currency equivalent of R200.00, plus
> - a percentage of the value of the policy investment at the time, plus
> - a percentage of the savings premium at the time (if applicable).
>
> These percentages depend on the size of the savings premium, the amount of the negotiated commission, and when payment of recurring premiums is stopped. At present, if payment of recurring premiums is stopped on or after the option date, no premium termination fee will be charged. We may change this from time to time."
>
> **"Can the policy lapse?**
>
> Yes. If recurring premiums are applicable, this will happen if payment of recurring premiums is stopped, or if permission to continue payment of recurring premiums is not re-obtained from the authorities, and the sum to which the value of the policy investment then has grown, less a premium termination fee as described above, is less than the minimum of the foreign currency equivalent of R1 500.00. If the member then already has turned 55, and there is an amount available, it will be paid to the member. The minimum will increase from time to time."

[8] The insurer seeks to justify the charging of a "premium termination fee" by arguing as follows:

> "The policy, it was agreed, would endure from 1 April 2002 until 1 April 2026.
>
> During this period contributions were to be made. From such contributions various costs would be deducted over the period.
>
> However, most of these costs were payable at the commencement of the policy ("upfront cost") and would be recouped over the life of the policy, unless the policy was terminated prematurely.
>
> As this policy was terminated only 13 months after commencement, the bulk of the premiums paid to the insurer was utilized to settle the upfront costs. Had the policy however continued as contracted until 2026, then the upfront costs would not have had a significant effect – as is the case in respect of the short period that actually elapsed."

[9] The fund states that it was not possible to combine the two policies as you had requested. The insurer, the fund argues, makes provision for switches between a variety of funds but since your policy was an offshore policy, the funds that you could have switched to were limited to a selection of international funds.

[10] The fund further contends that before applying for the policy a tax clearance certificate had to be obtained. The fund submits further that you were aware or ought to have been aware of the importance of obtaining a tax clearance certificate and that your policy would lapse should no contributions be paid. The fund seeks to rely on point 9 of the proposal document headed "Declaration by Life Assured" which provides, *inter alia*, that:

> "6. The life insured understands and notes that:
> - the life insured must obtain the tax clearance of the South African Revenue Service and must complete the SA Reserve Bank approval form (M.P.1423) in full and submit it with the proposal;
> - no premiums may be paid on the policy without the aforementioned clearance and approval;
> - as long as premiums are payable on the policy, the life insured must obtain a tax clearance certificate every 12 months or periodically as required by the South African Revenue Service, and as arranged by Sanlam Life in terms of existing practice that can change;
> - if, at any stage, official approval including but not restricted to the South African Revenue Service tax clearance and/or SA Reserve Bank approval is not obtained again, it will have the effect that no further premiums in respect of the policy can be paid. Depending on the number of premiums already paid at that stage, the policy could lapse. In such case, Sanlam Life will not be responsible for any claims, damages, losses or expenses that may arise from the said lapse;"

[11] The fund also seeks to rely, in this regard, on clauses of the policy document contained on page 4 of the document, which read:

> "**Permission from the authorities**
>
> **Is continuous permission from the authorities needed?**
>
> Yes. While recurring premiums are being paid (if applicable), permission is needed for the conversion of the rand amounts into foreign currency. This permission must be obtained from the South African Revenue Service and the South African Reserve Bank every 12 months, or as these authorities may otherwise prescribe.
>
> **What will happen to the policy if this permission is no longer granted?**
>
> The payment of recurring premiums will be stopped. … ."

Determination and reasons therefor

Technical point

[12] There is no merit in the technical point raised by the fund. The crux of this complaint does not constitute long term insurance business, but actually relates to a retirement annuity fund, which is a pension fund organisation

as defined in the Act. For the reasons more fully set out in *Schwartz v Central Retirement Annuity Fund and Another* [2005] 5 BPLR 435 (PFA) at paragraphs [12] to [28] and authorities referred to therein and *Louw v Central Retirement Annuity Fund and Another* [2005] 7 BPLR 622 (PFA) at paragraphs [17] to [36], I cannot uphold the contention that this matter constitutes "long term insurance business" over which I have no jurisdiction.

[13] This complaint is in fact a "complaint" as defined, in that it relates to the administration of the fund by the administrator and essentially alleges an act of maladministration in the instance through its levying of a charge the levying of which is not provided for in the rules. The decision in *Armaments Development and Production Corporation of SA Ltd v Murphy NO and Others* [1999] 11 BPLR 227 (C) at 231C puts it beyond doubt that a complaint concerning the maladministration of the fund by the person administering it or performing any of the functions prescribed in the Act or rules for such person, is a complaint as envisaged in the Act. Therefore this technical point cannot succeed.

[14] Furthermore, in so far as your complaint implicitly relates to the administration of the fund and/or the investment of its funds and it is implicit therein that you have suffered prejudice (in that your fund value has been wiped out) in consequence of the maladministration of the fund (in the form of the levying of undisclosed charges), your grievance constitutes a complaint as defined.

[15] Furthermore, Davis J (in whose judgment Le Grange AJ concurred) in the as yet unreported decision in *Central Retirement Annuity Fund v Adjudicator of Pension Funds, FE de Beer & Another*, Cape Of Good Hope Provincial Division Case No. 3404/05 (handed down on 20 October 2005) ("the de Beer judgment"), at page 9, confirmed the jurisdiction of this office and stated:

> "The basis of the complaint was that applicant [Central Retirement Annuity Fund] as the holder of the policy on the life of a member, was neither obliged nor entitled simply to allow Sanlam Life [the insurer] to charge whatever costs and charges it chose to levy and to accept whatever investment bonuses that it chose to declare from time to time without first satisfying itself through its own management committee of the reasonableness or adequacy thereof.
>
> The Rules of the Fund set out its essential purpose as being to provide benefits to members upon retirement. The fact that applicant may be exempt in terms of the applicable law from audit cannot exempt it from playing a role in the fulfillment of its purpose. In any event, applicant is a pension fund organization and has separate legal personality in terms of s51(a) [sic] of the Act. It cannot simply be treated as an illusionary 'go between' the members such as second respondent and Sanlam Life. It should be accountable to its members and hence be subject to the discipline of the Act's complaint mechanism."

[16] In any event, that your letter of complaint does not, in precise terms, make the averments required to constitute a complaint as defined is no reason by itself for a dismissal thereof as not constituting a complaint. Such an approach would be too formalistic, thus ignoring the purpose of the Act. The Cape High Court said the following in this regard in the *de Beer* judgment at page 9 and 10:

> "Applicant's contention regarding the second respondent's letter is based upon a formalistic reading of the complaints procedure as provided for in the Act. On this reading, the letter generated by second respondent would not constitute a proper complaint as defined. But this submission ignores the purpose of the Act. The structure of chapter VA of the Act is aimed at ensuring an effective, inexpensive and expeditious resolution of pension complaints by members, many of whom may not be able to afford legal advice and would therefore be compelled to formulate their complaint without any legal assistance or a complete understanding of the intricacies of the legal relationship between the respective parties, as in the case between Sanlam and applicant.
> In my view, second respondent's letter contains sufficient averments (as described above) to fall within the definition of a complaint. To construe a complaint as urged upon us by applicant would run counter to the very purpose of the complaints procedure provided for in the Act."

<u>The merits</u>

[17] At the heart of this complaint is the question whether the rules of the fund authorise the levying by the insurer of a "premium termination fee". Nowhere in the rules is there mention of such a fee or of any other fee when contributions are terminated prematurely.

[18] Rule 2 of Part 7 does not provide a definition of what constitutes "sufficient contributions" to have a policy made paid-up. No definition is further provided of what a "paid-up policy" is in the rules.

[19] The "Stratus International Retirement Annuity" summary document which was before me further includes a section on "Policy charges" where provision is made for the following additional costs to be recovered:

[19.1] marketing and administration charge
[19.2] policy fee
[19.3] yearly service fee
[19.4] yearly fund management fee
[19.5] statutory charges, including tax and stockbroker fees
[19.6] performance fee for the asset manager

[20] The fund, being a registered pension fund organisation, is bound by its rules, and can thus only do what its rules authorise it to do. There being no reference in the rules to the charging of any fee upon the premature termination of contributions, neither the fund nor the insurer may charge it.

[21] The clause in the policy document on which the insurer purports to rely provides that "the premium termination fee" consists of a sum of R200.00, plus an unspecified percentage of the value of the policy investment at the time, plus an unspecified percentage of the savings premium at the time.

[22] This non-disclosure of the applicable percentages (which are vague and open-ended) is compounded by the failure on the part of the insurer or the fund to give an indication of what the value of the policy investment was as at 1 May 2003 when the contributions ceased, and of the amount of the savings premium as at that date. This stands in stark contrast to the policy charges that are recovered (namely, marketing and administration charges, policy fee, yearly service fee, etc) as those are precisely stated on page 3 of the policy document.

[23] As the Supreme Court of Appeal held in *Tek Corporation Provident Fund and Others v Lorentz* [2000] 3 BPLR 227 (SCA) at paragraph [28], the trustees of a fund may do with the fund's assets only what is set out in the rules. The charging of a premium termination fee which exceeds the R200.00 that is stated in the policy document not being provided for in the rules nor precisely set out in the policy document, the insurer has no authority to charge it.

[24] With respect to the other leg of your complaint, it is apparent *ex facie* the policy document that switches can be made between "investment funds which are allowed for this type of policy investment at the time of switching". However, on the face of your proposal form and policy document it is clear that the investment selection was limited to a selection of international funds.

Relief

[25] In the result, I make the following order:

[25.1] It is hereby declared that the respondents had no right to deduct any amount from your investment account in the fund, over and above the R200 provided for in the rules of the fund, by reason only of you stopping contributions before your chosen retirement date.

[25.2] Sanlam Life Insurance Limited and the fund (the one paying, the other to be absolved) are jointly and severally ordered forthwith to credit your investment account in the fund with the R26 200.00 (less R200 for which the policy document expressly allows) that was debited therefrom together with interest on that amount, calculated at 15.5% per annum from the date of this determination until the date of crediting.

SIGNED IN JOHANNESBURG ON THIS DAY OF 2005

Yours faithfully

VUYANI NGALWANA
PENSION FUNDS ADJUDICATOR

Section 30M filing: Magistrate's Court