IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR
(HELD IN JOHANNESBURG)

CASE NO: PFA/WE/2908/05/CN

In the complaint between:

Johan Kannemeyer **Complainant**

and

Perpetua Retirement Annuity Fund **1st Respondent**

Capital Alliance Life Limited **2nd Respondent**

DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT 24 OF 1956

Introduction

[1] This complaint concerns the levying, by the administering insurer, of a "premium reduction adjustment" charge or fee against the complainant's investment account in the fund when he stopped paying contributions to the fund, in circumstances where neither the rules nor the policy document make provision therefor.

The facts

[2] The complainant started investing in the Perpetua Retirement Annuity Fund ("the fund"), whose business is administered by Capital Alliance Life Limited ("the administering insurer"), on 1 July 1997. The initial recurring monthly contribution was R125-00, which increased annually at the rate of the consumer price index. After he had made recurring contributions amounting to R9 852-46, the complainant informed the fund that he would cease contributing to the fund with effect from 1 September 2003. On 31 March 2005, the complainant was furnished with an information schedule reflecting, *inter alia*, that after the charging of a "Premium Reduction Adjustment" charge of R6 416-63 and "Alteration Fees" of R100-00, his net fund value as at that date was R6 381-44.

The complaint

[3] The complainant contends that it is not mentioned anywhere in the "policy documents" in his possession that the administering insurer may deduct unrecovered expenses from his contributions. He states that if he had been informed before "entering into this fund that, if for whatever reason, [he] stopped contributing to the fund after more than 6 years [he] would lose two thirds of the money invested, [he] would not have entered into the fund". He goes on to say: "The business of retirement funds should be to provide for the clients' future. If

companies are allowed to deduct costs at will as in this case, the process is fundamentally flawed."

[4] He requests assistance "to recover these penalties"

The responses

[5] A response has been filed by the administering insurer, while the fund has filed no response. The insurer explains that the "premium reduction adjustment" of R6 416-63 is the amount of "unrecouped expenses" that would have been recouped from the expense account over the full term of the complainant's membership, but because the contributions stopped before the contract had run its term of 31 years, the "unrecouped expenses" had to be debited to the investment account. As to how the expenses were made up, Mr. Nienaber explains as follows:

> **"Operation of investment and expense accounts**
>
> The investment portfolio of the policy is a smoothed bonus portfolio whereby all expenses based on the term of the policy are transferred to the expense account of the policy. Expenses (unrecovered costs) are made up of the initial and renewal commission, plus the initial policy acquisition costs and monthly renewal expenses expressed in rand value.
>
> The investment portion (95%) of each premium is transferred to the investment account of the policy at each specific transaction date. Smoothed up-front-declared bonuses (i.e. in essence the growth of the portfolio) are added monthly to both the investment and expense accounts.

Please note that the portfolio return is applicable to both accounts.

The unallocated portion (5%) of each premium received is credited to the expense account and the expense account will be zero at the maturity date of the policy.

The fund value of the policy, at any given point in time, is determined by the following. The accumulative amount of the allocations from premiums received plus bonuses declared, in the investment account, minus the accumulative amount of the expenses minus the unallocated portion (5%) of each premium received plus the declared bonuses held in the expense account.

The above is applicable to each premium increase, based on the remaining term of the contract."

[6] According to the "DETAILED POLICY INFORMATION SCHEDULE" that was furnished to the complainant in March 2005, his fund value was calculated as follows:

"Summary of Value Breakdown as at Thu Mar 31 09:25:34 2005

Premiums Allocated to Investment	R9 852-46
Growth on Investment	R2 745-61
Special Bonuses	R 300-00
Alteration Fees	R -100-00
Premium Reduction Adjustment	R-6 416-63
Net Fund Value	**R6, 381.44"**

[7] Mr. Nienaber argues that a provision of the policy, contained in a document entitled "Summary of General Provisions Affecting the Member of the Perpetua Retirement Annuity Fund", as well as Rule 7 of the fund, authorize it to debit unrecouped expenses to the member's investment account. He goes on to state that the expenses are based on the standard practice in terms of this "type of policies" and that the commission was paid in terms of the Long Term Insurance Act and vested in full after twelve months from date of payment.

Determination and reasons therefor

[8] It comes as a relief that no technical arguments like lack of jurisdiction have been raised in this matter. So then I go straight to dealing with the merits. The provisions of the policy document on which the insurer claims to rely are to the following effect:

> **"Provisions**
>
> **Introduction**
>
> This membership certificate is issued in terms of the rules of the Perpetua Retirement Annuity Fund ("the fund"). This summary is included for the member's information and does not confer any rights apart from the rules of the fund, the master policy issued to the fund, and the schedule of this certificate".

> **"Non-payment of contribution**
>
> If any payment is due and unpaid then this Retirement Annuity will be made paid up. All risk benefits will continue to reflect the investment performance (if unit linked) or will continue participating in bonuses (if Smoothed Bonus Fund).

[9] There is no definition of the term "paid-up" in the document, nor are the implications of the policy being made paid-up explained. Save for a paragraph relating to risk charges, there is no mention of any costs, fees or charges of any other nature in the entire document. The paragraph in question reads as follows:

> **"Risk Charges**
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> A member may be covered by various risk benefits such as death or disability benefits. In such cases, Norwich Life will calculate the costs of these benefits every month and will debit the Investment Account (the Vesting Account in the case of the Smoothed Bonus Fund) with these costs. Norwich Life does not guarantee that the rates at which those charges are made cannot change, and reserves the right to charge them."

[10] The Schedule merely sets out the following information: the commencement date of membership; the "expiry date"; the nature of the benefit; the contribution amount; the applicant's names; age and date of birth and the application date. There is no mention of any costs, fees or charges whatsoever.

[11] Rule 7 which deals with the discontinuance of contributions provides as follows:

> **"DISCONTINUANCE OF CONTRIBUTIONS**
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> If a MEMBER discontinues his contributions to the FUND prior to his RETIREMENT DATE his assurance under the MASTER POLICY shall be converted to a reduced fully paid-up assurance of an amount as determined by the INSURER, based on the contributions to be applied at the MEMBER'S RETIREMENT DATE towards the purchase of an annuity on his life.
>
> Any MEMBER who has discontinued his contributions may resume contributions to the FUND in return for such benefits and subject to such conditions as the INSURER may stipulate, including, if applicable, the furnishing of satisfactory evidence of insurability."

[12] The insurer argues that the phrase "shall be converted to a reduced fully paid-up assurance of an amount as determined by the insurer, based on the contributions" authorizes it to debit "unrecouped expenses" to the complainant's investment account. The use of the phrases "assurance" and "fully paid-up assurance" in the rule, read together with the clause in the policy document dealing with non-payment of contributions (quoted in paragraph [8] above) appears to authorize the payment of a reduced life or disability benefit ("risk benefits"), and does not authorize the reduction of the value of a member's fund value. Even if my interpretation in this regard is incorrect, at the most the rule can only be read to allow for the payment of a reduced benefit the amount of which shall be determined by the insurer with reference to the contributions paid. A retirement annuity fund may only pay out a benefit when a member reaches retirement age, or dies, or has become disabled.

None of these has occurred in this case, thus the complainant's fund value or amount in his investment account may not be reduced as a result of his having stopped paying contributions because his fund value at this stage is not a "benefit".

[13] The rules and the policy being silent on the deduction of the premium reduction fee of R6 416-63, the insurer cannot deduct those charges from the complainant's investment account simply because it is "the standard practice in terms of this type of policies issued". It is this reliance on "practice" rather than prescribed statutory and contractual provisions that attracted the umbrage of the Supreme Court of Appeal in *Mostert NO v Old Mutual Life Assurance Company (South Africa) Ltd* [2001] 8 BPLR 2307 (SCA), where Smalberger ADCJ remarked as follows at paragraphs [67]-[72]:

> "[67] …The second argument is that there existed a practice, which had superseded the law, in terms of which the rules and registered status of a fund could be altered by an employer (again in the case of a scheme) without any formal amendment of the rules and without registration of any amendment.
>
> [68]…….
>
> [69] The second argument is also designed to get awkward provisions out of the way. The gist of it is as follows. The office of the Registrar, as the evidence indicates, is understaffed. It is required to deal with a great number of funds. If it were to operate according to the prescribed statutory requirements there would be inordinate delays. They provide that amendments to the

rules do not take effect until they are registered (although they may be registered with retrospective effect). As a change of status from a wholly underwritten to a privately administered fund requires changes to the rules, such a change can only occur once the appropriate rule change has been registered. In order to cope with the inconveniences which an adherence to the statutory requirements would involve, a practice has evolved, so the argument runs, to which the Registrar's office is a party, in terms of which informal amendments effected by the employer, are treated as having full legal effect, without submission to the Registrar, and without registration by him….

[70]……

[71]….The provisions of the Act regarding the filing, registration and effect of rules are perfectly clear, as is also their purpose. There is no basis for contending that these provisions have been repealed or were entitled to be ignored because of some "practice".

[72] Once …the abrogation of the statutory regime [is] rejected, then it seems clear that if Old Mutual had complied with the conditions of exemption, the rules of the Fund and the policy, the payments to CAF in December 1994 would not have been made. However, if its thinking at the time accorded with that reflected in the argument presented on its behalf (we do not know whether it did, as no evidence was given), then it is unsurprising that events took the course they did. Mr. *Gauntlett*, for Mostert, has typified these arguments on behalf of Old Mutual as cynical. There is much to be said for that".

[14] The Supreme Court of Appeal's judgment in *Tek Corporation Provident Fund and*

Others v Lorentz [2000] 3 BPLR 227 (SCA) at paragraph [28] is authority for the proposition that what the trustees may do with the fund's assets is set forth in the rules, and that if what they propose to do is not within the powers conferred on them by the rules they may not do it. Section 13 of the Act also emphasizes the binding effect of the rules of a fund. In what appears to be an internal e-mail correspondence dated 18 June 2004 there is even talk of a "surrender penalty". This "penalty" is not provided for anywhere in either the rules or the policy documents and can thus not be imposed on the complainant.

[15] There is therefore no basis for the deduction of any expenses other than those detailed in the rules and the policy document from the complainant's contributions.

Relief

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

[16.1] The Perpetua Retirement Annuity Fund and Capital Alliance Life Limited are ordered jointly and severally (the one paying, the other to be absolved) to credit the complainant's investment account in the fund with the amount of R6 416-63.

[16.2] The Perpetua Retirement Annuity Fund and Capital Alliance Life Limited are

further ordered to pay interest on the amount referred to in paragraph [15.1] above at the rate of 15.5% per annum, from the date of this ruling until the date of final payment.

DATED AT CAPE TOWN THIS DAY OF 2005.

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VUYANI NGALWANA
PENSION FUNDS ADJUDICATOR

Appearances
All parties unrepresented

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SECTION 30M FILING: MAGISTRATES'COURT