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Please quote our ref: PFA/KZN/2912/05/KM

Dear Sir,

**RE: DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT 24 of 1956 (“The Act”): J. HORSFIELD v CENTRAL RETIREMENT ANNUITY FUND (“the fund”) & SANLAM LIFE INSURANCE LIMITED (“Sanlam”)**

Introduction

- [1] Having considered the complaint that was received by this office on 23 March 2005, as well as further written submissions, I consider it unnecessary to hold a hearing in this matter. My determination and reasons therefor appear below.
- [2] As the facts are well-known to all parties I shall not burden this ruling by repeating them in detail here.

The complaint

- [3] Your complaint concerns the calculation of the value of your investment account in the fund after you had ceased making contributions to the fund. You paid contributions totalling R18 214 from March 1990 to March 2000, after which you had to cease payments due to changed financial circumstances. You were advised by Sanlam that you could not “cash in” the policies, but that you could cease contributions and claim your benefit

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V Ngalwana (Adjudicator), N Jeram (Deputy Adjudicator), C Nkuhlu (Snr Assistant Adjudicator), L Shrosbree (Snr Assistant Adjudicator), Z Camroodien (Snr Assistant Adjudicator), F Mtayi (Snr Assistant Adjudicator), K MacKenzie (Snr Assistant Adjudicator), N van Coller (Assistant Adjudicator), L Mbalu (Assistant Adjudicator), R Maharaj (Assistant Adjudicator), J Mabuza (Assistant Adjudicator), V Abrahams (Assistant Adjudicator), Solomzi Gcelu (Assistant Adjudicator)

Office Manager: L Manuel

when you turned 55. In April 2004, having turned 55, you were eligible for a benefit from the fund, but were dismayed to find that the value was only half of what you had paid in, and you were paid out R9 223. You are upset at what you perceive as a very poor return on your retirement savings, and have therefore approached this tribunal for assistance.

### The responses

- [4] In its response, the fund raises the point that the Adjudicator lacks jurisdiction to investigate this complaint as it pertains to long-term insurance business. On the merits, it explains that the reduction in your fund value was attributable to the cost of the risk benefits that you elected to include (death and disability), as well as an “alteration fee” that was applied when your contributions ceased, and a further early termination fee applied when you retired earlier than agreed.
- [5] The fund states that the only option available to you when you could no longer continue paying recurring contributions prior to age 55 was to have the policy made paid up. It then goes on to explain that most of its upfront expenses were incurred at the commencement of the policy and would be recouped over the life of the policy unless it was altered before its maturity date. If contributions stop prematurely, which means the premiums on the underlying policy also cease, a large portion of the upfront expenses will no longer be recovered from future policy charges. Sanlam therefore charges an alteration fee when the policy is made paid up.
- [6] The fund relies on clause 9 of the section Description of Provisions of the policy document, which stipulates as follows:
- “If a premium is not paid within the period of grace, the policy shall be converted into a paid-up policy for reduced benefits according to the practice of Sanlam”.
- [7] In your case, this resulted in the following situation:

Balance of investment account before policy was made paid up	=	R14 260.44
less policy alteration fee	=	R 5 264.09
Balance of investment account after Policy was made paid up	=	R 8 996.35

- [8] In addition, the risk benefits that you elected to include had the following impact on your fund value:

Total amount of contributions paid	=	R18 068
Total cost of risk cover	=	R 7 963
Available for investment	=	R10 105

- [9] The fund also reports that because you retired earlier than originally planned a further early termination fee was debited against your account. The resulting impact on your fund balance is reflected in the response as follows:

Balance of investment account before		
Early retirement	=	R11 783,76
Less early termination fee	=	R 1 483,27
Less market adjustment fee	=	R 824,04
Balance of investment account after		
Early retirement	=	R 9 476,45

- [10] The fund explains the above reductions as follows:

“For policies in the smooth bonus series bonuses are declared on a yearly basis to smooth the return the client will receive. On early termination the insurer pays the lesser of the smoothed value of the policy and the underlying market value of the policy. If the insurer did not do this, policyholders in this investment fund could terminate their policies when markets are down as they will get the higher smoothed value. This value is therefore adjusted to reflect the underlying market conditions.”

- [11] Sanlam has also filed a response in its capacity as administrator of the fund. In that response, the provisions relied on for the alteration and termination fees are set out. The *in limine* point of jurisdiction of this office to entertain the complaint has once again been taken, for the same reasons given by the fund.

#### Determination and reasons therefor

- [12] There is no merit to the preliminary point raised by the respondents. 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 organization as defined in the Act. For the reasons more fully set out in *Schwartz v Central Retirement Annuity Fund & Another* [2005] 5 BPLR 435 (PFA) at paragraphs [12] to [28]. I cannot uphold the contention that this matter constitutes “long term insurance business” over which I have no jurisdiction.
- [13] On the merits, it appears that the investment portion of your retirement funding was substantially reduced by the cost of risk benefits. That is a cost to which you agreed, and was therefore lawfully deducted from your contributions.
- [14] I now turn to the provisions on which the respondents rely for effecting the deductions in respect of cessation of contributions and early retirement.

[15] Rule 2 of Part 7 provides:

“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. The MEMBER will then have the right to apply for reinstatement of his benefits, partially or in full, and the MANAGEMENT COMMITTEE in consultation with the ASSURER will consider such a proposal on receipt of.....”

There is no definition of what a “paid-up policy” is in the rules, and certainly no mention that in converting the policy to a paid-up policy for reduced benefits the insurer may charge a “premium termination adjustment” fee. I have not been referred to, nor can I find any authority in the policy document for such a fee.

[16] As matters stand therefore, neither the rules nor the policy documents authorize the insurer to charge a policy alteration fee. There is similarly no authority in either the rules or the policy document for the application of an early termination fee on retirement earlier than initially indicated. The payment of underlying market value (the debit of R824,04) on early termination of membership is a device aimed at anti-selection designed to protect the remaining members. As such I do not find it unreasonable.

[17] Part 8 of the rules governs benefits and modes of payment. On your retirement date, you became eligible for a pension payable for life. However, several options arose with regard to how this benefit was applied. In terms of rule 1.4.1 the pension could be purchased from the assurer with the fund as owner. In terms of rule 1.4.2 the pension could be purchased from a registered assurer of your choice with you as the owner of the policy. Rule 3.1 offers a further alternative in terms of which you were permitted to commute a maximum of one third of your pension to a lump-sum. However, should the pension not exceed R1 800 per annum (as is the present case) you were entitled to commute the full pension, which you elected to do. In view of the unlawful deduction of fees by reason of your stopping contributions, which could well have affected the value of your benefit, you are entitled to re-elect on the basis of a higher benefit the option that best suits you.

[18] In the result I make the following order:

[18.1] The Central Retirement Annuity Fund is ordered forthwith to calculate the amount that would have been available for the purchase of a pension, had the policy alteration fee and the early termination fee (relating to the paid-up benefit and early retirement



***SECTION 30M FILING: MAGISTRATES' COURT***