



HEAD OFFICE  
Johannesburg  
1<sup>st</sup> Floor, Norfolk House  
Cnr 5<sup>th</sup> Street & Norwich Close  
Sandton, 2196  
PO Box 651826, Benmore, 2010  
Tel (011) 884-8454 □ Fax (011) 884-1144  
E-Mail: [enquiries-jhb@pfa.org.za](mailto: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](mailto:enquiries@pfa.org.za)  
Website: [www.pfa.org.za](http://www.pfa.org.za)

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Please quote our reference: PFA/WE/4358/2005/NVC

**Re: DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT 24 of 1956 (“the Act”): E J Strydom v Central Retirement Annuity Fund (“the fund”) and Sanlam Life Insurance Limited (“Sanlam” or “the insurer”)**

Introduction

- [1] Your complaint concerns the value of the retirement benefit that you received when you advanced your date of retirement. The complaint was received on 19 July 2005 and a letter acknowledging receipt thereof was sent to you on 5 August 2005. On the same date letters were dispatched to the respondents requesting them to submit responses to your complaint by 29 August 2005. The responses dated 29 August 2005 were received on the same date. On 6 September 2005 the responses were sent to you for a reply by 23 September 2005. Your reply was received on 19 October 2005.
- [2] In December 2005 an announcement was made of a Statement of Intent between the Minister of Finance, on the one hand, and the Life Offices Association and five large life assurers on the other, in terms of which the life assurers would commit themselves to certain minimum standards in respect of retirement annuity funds and endowment policies. Although the statement is not binding on this office, we nevertheless referred all retirement annuity fund complaints (including this one) back to the management boards and life assurers administering these funds with a view to facilitating an amicable resolution of the complaint between the parties without the intervention of this office. This matter was referred for settlement to the fund on 20 January 2006. The parties were given 30 days to settle the matter failing which this office would determine the complaint in the ordinary course. Many complaints were settled on this

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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), R Maharaj (Snr Assistant Adjudicator), N van Coller (Assistant Adjudicator), L Mbalo (Assistant Adjudicator), J Mabuza (Assistant Adjudicator), V Abrahams (Assistant Adjudicator), S Gcelu (Assistant Adjudicator), T Thabethe (Assistant Adjudicator), M Ramabulana (Assistant Adjudicator)

Office Manager: L Manuel

basis but the settlement terms were not divulged to this office. However, on 23 February 2006 we were informed that the parties in this complaint had failed to reach a settlement in this case. The details of disagreement were not communicated to us. It is with that brief background that we now determine this complaint in the ordinary course. My determination and reasons therefor appear below. As the facts are known to the parties I shall only repeat those facts that are pertinent to understanding this determination.

### Factual Background

- [3] You commenced contributing to the fund when you were 44 on 1 November 1986 at the monthly rate of R55, increased to R255 with effect from 1 July 1997. Your elected retirement date was 1 November 2008, but you decided to accelerate it to 1 March 2003, when you reached 60. The retirement value was R29 632.08 from which you received a cash lump sum of R9 877.37 and an annual pension of R1 018.66. The total contributions to the fund amounted to R25 040.00.

### Complaint

- [4] You contend that this investment is the “poorest investment imaginable” and you are particularly unhappy that:
- [4.1] You did not receive the benefits projected by Sanlam at inception of the policy. It had projected that your retirement benefit would be R138 393 at the age of 65 and R55 782 at 60. You want Sanlam to reimburse you with the difference between R55 782 and R29 632.08 received, when you retired at the age of 60 on 1 March 2003;
  - [4.2] The costs recovered by the respondents represent 49.69% of the contributions that you made to the fund; and
  - [4.3] The annuity which you have been receiving for the last five years has not increased and you want Sanlam to increase it in terms of prescribed minimum increases to pensions.

### The response

#### Technical points

- [5] The fund and the insurer have raised two technical points in response to the complaint, and have also dealt with the merits. The first technical point is that this is not a “complaint” as defined in the Act as it is not about the execution of duties by the fund (or administrator). Instead, they contend

that the dispute concerns the execution of duties by the insurer under the policy, notably the actuarial substructure of the policy, which constitutes long-term insurance business as defined in, and regulated under, the Long-Term Insurance Act.

- [6] The second technical point is that because this complaint is not about maladministration of the fund by the fund (or the administrator), it is not a “complaint” as defined in the Act.

### Merits

- [7] On the merits, the fund states that rule 2 of Part 7 stipulates that contributions are payable during the period determined in the policy issued on the member’s life and if this is not done, the policy obtains a paid-up value for reduced benefits. It states that as the fund holds no assets other than claims against the insurer, it is unable to enhance the surrender value of a policy.
- [8] It also contends that in terms of rules 4 and 5 of part 8, the liability of the fund is restricted to the value in the policy and the overall liability of the insurer is determined by the conditions of the policy.
- [9] The respondents maintain that the illustrative values do not constitute contractual promises and that the policy documents advise that the final benefits would depend on actual growth rates, cost recoveries and the basis of calculation from time to time. Further, the insurer points out that the policy documents state that, at the acceleration of the retirement date, Sanlam will decide on the value of the benefit, at which time it reduces the benefit by making an early termination adjustment in order to recoup the unrecovered costs.
- [10] Sanlam states that most of the expenses in respect of a policy are incurred at inception and recovered over the contractual period of the contributions. If contributions cease prematurely, the expenses are recovered by an early termination adjustment.
- [11] Sanlam states that the adjustment of R5 221.85 was made to allow for the fact that the market value of the investment portfolio was, during February 2003, at a low level relative to the book value of the underlying assets of the policies in the portfolio. Benefits for members who retire early are adjusted to prevent their leaving the fund early to the detriment of those remaining up to their contractual retirement dates.
- [12] Sanlam advises that the costs attached to the policy were R10 348.68, broken down as follows:

“Total paid-in premiums up to 28/02/2003	R25 040.00
Less: Total policy fees and administration charges	R 2 094.31
Less: Total risk premiums	R 1 266.31
Equals: Premiums available for investment	R21 697.38
Plus: Investment return up to 28/02/2003	R18 301.38
Fund Value of policy on 01/03/2003 prior to early termination	R39 980.76
Less: Early termination adjustment	R10 348.68
Early retirement benefit on 01/03/2003	R29 632.08”

[13] Sanlam states that the early termination adjustment was calculated as follows:

“R 5 126.83 - recoupment of upfront costs due to advancement of retirement date  
R 5 221.85 – market value adjustment  
R10 348.68”

[14] Sanlam concludes that the fees and the maturity values, calculated prior to the elected retirement dates, were calculated according to sections 46, and 52(3) of the Long-Term Insurance Act, which deal with the failure to pay premiums. These sections in particular require that a policy must be actuarially sound, and for the calculation of a policy value where the member reduces or prematurely discontinues the contributions.

[15] In respect of your second complaint that your pension has not increased over the past five years, Sanlam responds that the pension that you are receiving is in line with the option that you exercised on 3 February 2003, namely, that you accepted a fixed pension of R1 018.66 annually. It adds that there is no legislation in place to compel Sanlam to increase the pension.

#### Determination and reasons therefor

##### Technical points

[16] There is no merit in the technical points 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 and Another* [2005] 5 BPLR 43 (PFA) at paragraphs [12] to [28] and authorities referred to therein and *Louw v Central Retirement Annuity Fund and Another* [2005] 7 BPLR 363 (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.

[17] Furthermore, Davis J (in whose judgment Le Grange AJ concurred) in *Central Retirement Annuity Fund v Adjudicator of Pension Funds and Others* [2005] 8 BPLR 655 (C) at 660C - E confirmed the jurisdiction of this

office and stated:

“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 illusory ‘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.”

[18] 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 investment value has reduced) in consequence of the maladministration of the fund (by the levying of undisclosed charges), your grievance constitutes a complaint as defined. (See *Louw* (cited above) at paragraphs [11] to [15].)

[19] Both technical points are therefore dismissed.

### Merits

#### Projected maturity value

[20] The first issue for determination is whether you are entitled to the benefits projected by Sanlam at inception of the policy or at any other time. Under “Voorbehoue en Veronderstellings” in the policy document it is stated that the benefits will be determined by the actual bonus rates and calculation basis applicable from time to time. Once you decided to invest in a market-related portfolio, you carried the investment risk. This means that you benefited from a surge in the market and carried the loss in periods where the market was in decline. I am satisfied that the values were not guaranteed and depended on actual growth rates, annuity rates and inflation rates.

[21] According to Sanlam investment returns in general move with the inflation rate. In 1997 the illustrated rates of return of 14% and 11% were in line with investment returns earned and inflation rates at that time. It states the decline in the inflation rate from 1997 impacted on investment returns, reducing them from 8.6% in 1997 to 5.8% in 2003.

[22] Furthermore, although you are aggrieved about the poor investment, you have not suggested that the board was negligent in terms of the investment decisions taken, or that there was a failure to adopt specified investment strategies. In view of the above, you have failed to establish any entitlement to relief in respect of this aspect of your complaint.

#### Early termination penalty

- [23] The second issue for consideration is whether the rules of the fund authorize the levying by the fund or Sanlam of an adjustment for the unrecovered expenses of R5 126.83, also referred to as an early termination adjustment, in view of your advancing your retirement date from 1 November 2008 to 1 March 2003.
- [24] Rule 2 of part 7 states:
- “Term of contributions  
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...”
- [25] There is no definition of what a “paid-up policy” is in the rules, and certainly no mention that in terminating the contributions prior to the contractual retirement date the insurer may charge an early termination adjustment.
- [26] Clause 9 of the policy document deals with “paid-up policies” and provides that if premiums are not paid within the period of grace the policy will become paid-up with a reduced value in accordance with the insurer’s practice, but does not specify how the reduced benefits would be computed.
- [27] Neither the rules of the fund nor the policy documents provide for the levying of an adjustment for unrecovered expenses or an early termination adjustment of R5 126.83.

#### Market value adjuster

- [28] The next issue concerns the deduction of the market value adjustment of R5 221.85. This is also known in the industry as a “market value adjuster” (“MVA”) and is applied to a fund share when its face value is higher than the market value of the underlying assets. The background and application of these MVA’s particularly in the context of “with profit” annuities, was fully set out in a previous determination of this tribunal, *Mungal v Protektor Preservation Fund and Old Mutual Life Assurance Company (South Africa) Limited*, as yet unreported, case number PFA/KZN/2658/KM, dated 29 May 2006, at paragraphs [21] to [31].

- [29] Neither the rules of the fund nor the policy documents provide for the levying of an adjustment for market value of R5 221.85.
- [30] Section 13 of the Act sets out the binding force of the rules. As the Supreme Court of Appeal stated in *Tek Corporation Provident Fund and Others v Lorentz* [2000] 3 BPLR 227 (SCA) at paragraph [28] the trustees may only do with the fund's assets what is set forth in the rules. Thus, if what they propose to do is not within the powers conferred on them by the rules, they may not do it.
- [31] The trustees of the fund are, moreover, under a duty to ensure that the terms of any underlying contract taken out in respect of, and for the benefit of, a member are adhered to by the other contracting party. They may not simply wash their proverbial hands of all responsibility. Section 7C of the Act codifies the common law fiduciary duty owed by trustees to the beneficiaries on behalf of whom they hold trust assets. In this sense members are in a similar position to trust beneficiaries. Section 7C provides that the object of a board shall be to direct, control and oversee the operations of the fund in accordance with the applicable laws and rules of the fund. Nothing in the rules and the Act allows for the deduction of an early termination adjustment or the MVA.
- [32] As Davis J stated in the *De Beer* judgment (at 660D-E), the fund cannot simply be treated as an illusionary go-between between the members and the insurer. It should be accountable to its members and hence be subject to the discipline of the Act's complaint mechanism. On the issue of the charges levied by the insurer, Davis J stated as follows (at 663E-G):
- "It follows that the reasonableness of the total charges levied by the insurers from time to time in respect of the administration of the fund and the apportionment thereof among beneficiaries are considerations of which account must be taken by Applicant's management committee. Similarly, the reasonableness of investments effected and maintained by the insurer for the fund from time to time should be examined by the management committee, if the latter is to fulfill its fiduciary responsibilities to members. In addition, the adequacy of disclosure of information which is critical to the interests of members, such as an adequate and fair explanation as to the meaning of documents which provide illustrative values at the inception of the contract as well as the adequacy of disclosure by the insurer to members from time to time, must, in the light of the analysis advanced, comprise part of the responsibilities of the management committee of applicant."
- [33] For the above reasons, I am satisfied that the fund was not entitled to permit the above deductions to your benefits since it was not authorized by the rules or by the terms of the policy between the fund and the insurer. Because this reduction of the benefit was effected by and for the benefit of Sanlam in circumstances where the policy document does not allow therefor, the order in that regard must be directed at Sanlam.

### Pension increases

- [34] The final aspect of your complaint concerns your entitlement to pension increases. The Act prescribes that after the commencement of the new surplus legislation on 7 December 2001, within a certain period, all funds must establish a policy regarding pension increases to pensioners.
- [35] The minimum pension provisions in the Act essentially require that every pension fund organization must establish and implement a minimum pension increase policy which must aim to award a percentage of the consumer price index (CPI) or some other measure of price inflation which is deemed suitable and also deal with how often the increases will be granted. The minimum pension increase is then, in simple terms, the minimum of inflation-related increases (as set out in the minimum pension increases policy aforementioned) and increases that can be afforded.
- [36] The Act specifically states that the pension increase policy must *aim* to award a percentage of the CPI or some other measure of price inflation. Furthermore the Act includes affordability as a factor in the determination of the “minimum pension increase”. In other words the Act does not prescribe what the minimum pension increase should be. The board has a discretion to determine the appropriate pension increase to be awarded with reference to affordability and its pension increase policy.
- [37] The fund has responded that the investment that you elected did not provide for increases. The fact that the indications were strong from the structure of the underlying investments that increases will not be affordable does not relieve the fund of the statutory obligation to record the circumstances and its consequent position in a formal policy.

### Relief

- [38] The order of this tribunal is as follows:
- [38.1] It is hereby declared that the respondents were not entitled to levy the charges of R5 126.83 and R5 221.85 respectively as an early termination adjustment and a market value adjuster on your investment value solely by reason of your exiting the fund some five and a half years earlier than your selected retirement date.
- [38.2] Sanlam is directed to pay to you, or transfer to an institution of your choice, in accordance with the applicable rules and legislation, the amounts referred to in paragraph [38.1], within six weeks of the date of this ruling.

[38.3] Sanlam is further ordered to pay interest on the amount of the payment or transfer in paragraph [38.2] at the *mora* rate of 15,5% per annum reckoned from 1 March 2003 until date of transfer or payment.

[38.4] The fund is hereby directed to formulate a policy in terms of section 14B(3) of the Act, and communicate same to you, within four weeks of the date of this determination.

[38.5] The complaint relating to projected maturity values is dismissed.

Dated at Cape Town on this the                      day of                      2006.

Yours faithfully

**Vuyani Ngalwana**  
**Pension Funds Adjudicator**