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Please quote our ref: PFA/WE/3813/05/CN

**RE: DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT, 24 OF 1956 (“the Act”): JM VAN RENSBURG v CENTRAL RETIREMENT ANNUITY FUND & SANLAM LIFE INSURANCE LIMITED**

**INTRODUCTION**

1. This matter concerns the apparent fluctuations in the illustrative maturity value of the retirement benefit of a member of a retirement annuity fund, as well as the application, by an insurer, of a factor known as a “market value adjuster” to re-adjust the value of the retirement benefit due to a member who retires prior to the contractual retirement date.
2. The complaint was received by this office on 2 June 2005, and a letter acknowledging receipt thereof sent to you on 14 June 2005. On the same date a letter was dispatched to the respondents giving them until 5<sup>th</sup> July 2005 to file a response to the complaint. The responses dated 5 July 2005 and 25 July 2005 were received on 5 July 2005 and 28 July 2005, respectively. The response dated 5 July 2005 was sent to you on 13 July 2005 for a reply by 27 July 2005. The respondent sent you a copy of the second response. A reply was received from you 22 July 2005. After considering the written submissions before me, I consider it unnecessary to hold a hearing in this matter.
3. 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

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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

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.

4. This matter was referred for settlement to the Central Retirement Annuity Fund and Sanlam Life Insurance Limited on 19 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 basis, but the settlement terms were not divulged to this office. However, on 24 February 2006, we were informed that the parties to this complaint had failed to reach a settlement in this case. The details of disagreement were not communicated to us.
5. It is with that brief background that we now determine this complaint in the ordinary course.

#### THE FACTS

6. You joined the Central Retirement Annuity Fund (“the fund”), which is administered by Sanlam Life Insurance Limited (“the insurer”) on 1 September 1983, and elected 1 September 2007 as your retirement date. Your initial monthly contribution was R253.00, which you increased to R411.22 on 1 January 2001.
7. On 1 November 2004, you decided to advance your retirement date, at which point you had already paid contributions amounting to R70 395 38. Investment return in the sum of R225 859.01 was credited to your investment, and an early retirement benefit of R296 254.39 became available for you to purchase an annuity. You elected to transfer the entire benefit to the South African Retirement Annuity Fund.

#### THE COMPLAINT

8. Having regard to the illustrative maturity value of R526 263.00 that was quoted to you in a statement of assurance dated 5 December 2002, a further statement dated March 2003 (where the investment value was stated as being R296 560) and a Policy Schedule that was prepared for you by your independent broker on 27 October 2004 (stating the policy value as being R364 540), you are not satisfied with the apparent fluctuation in the value of your investment, and particularly with the amount of the early retirement benefit (R296 254.38) that became available on 1 November 2004.
9. You also want the insurer to explain “what happened to the plus minus

R70 000”, which you allege is the difference between the policy value as at 27 October 2004 and the early retirement benefit.

## THE RESPONSES

### Technical points

10. In a joint response the fund and the insurer have raised two technical points that your grievance is not about the execution of duties by the Fund (or the administrator), but is about the execution of duties by the insurer under the policy (namely about the internal operation of the policy, notably the operation and application of the actuarial rules of the policy) which constitutes “long-term insurance business” as defined in, and regulated under the Long Term Insurance Act.
11. They further argue that your complaint does not constitute “a complaint” as defined in the Pension Funds Act, in that, in particular, it is not about the maladministration of the fund by the fund or the administrator.

### The merits

12. On the merits, the insurer states that from your total contributions of R70 395.38, commission of R2 614.39 was paid (for the first two years after membership commenced and for the first two years after the contributions were increased).
13. It further states that the policy that was taken out on your life was a policy in the Reversionary Bonus Series which, unlike the more conventional policies, by its nature does not have an expense account. The insurer explains that such policies operate in the following fashion: When membership commences, a sum assured for the policy is calculated (which in your case was R79 523 at inception), based on certain conservative assumptions, like the insured’s age, the term of the policy at inception and the expected amount of premiums that will be received over the term of membership.
14. According to the insurer, depending on whether the insurer’s investment return is better than what is reflected in the calculation of the sum assured, the insurer can declare two types of bonuses: reversionary (vesting) bonuses and claim (non-vesting) bonuses. The former are declared annually in the form of a percentage of the sum assured and a percentage of the already vested bonuses and are added to the policy. The latter are also declared annually, but are a percentage of the existing reversionary bonuses and a percentage of the sum assured. They are however not added to the policy, can reduce in subsequent years and thus do not form a permanent part of the policy’s benefits. Claim bonuses are only paid out in the event of a claim during that year. It is only if contributions are received until the policy has endured until the chosen retirement date that

- a member can receive the full sum assured and the allocated bonuses.
15. If however the member chooses to retire after his/her 55<sup>th</sup> birthday as s/he is entitled to, the present value (discounted value) of the sum assured plus the already declared bonuses are calculated, and the value is then multiplied by a market adjustment factor to make provision for the market value of underlying assets in the portfolio.
  16. With regard to the amount of the benefit that became available to you upon your early retirement, the insurer states that the total sum assured plus bonuses that would have been paid to you had your membership endured until 1 September 2007 would have been R415 888.71. However, because the benefit was paid out earlier, that amount had to be discounted to the current date (1 November 2004) by effecting an adjustment of R86 717.17, which equals the difference between the value of the sum assured plus bonuses payable at maturity date and their value at early retirement. The insurer goes on to submit that the adjustment is not a deduction of fees or due to costs, but is simply due to discounting a value payable at a future date to the early retirement date.
  17. According to the insurer, a further adjustment of R32 917.15, known as the “market value adjustment”, was made to ensure that the sum assured plus bonuses, less the first adjustment, for all similar reversionary bonus policies, do not exceed the actual assets held for those policies, which would be to the detriment of remaining policyholders. The insurer states that the first adjustment represented 21% of the sum assured plus bonuses, while the second one was equal to 10% of the sum assured plus bonuses less the first adjustment. It concludes that in November 2004, the total sums assured plus bonuses, less the first adjustment, for all similar reversionary bonus policies was 109% of the market value of the assets held for those policies, and that after the subtraction of the second adjustment of 10%, you received 99% of the asset share of the policy.
  18. Regarding the illustrative maturity values, the insurer argues that the amount of R364 540 that was stated as being the policy value as at 27 October 2004 was a misstatement by your broker, for which it cannot be held liable, and that the correct policy value as at that date was R362 608.30. Further according to the insurer, the illustrative values were based on the assumptions that the monthly contributions would be paid until the retirement date and that the illustrative growth rate used in the calculations would apply until retirement date. It further states that an illustrative maturity value is not guaranteed and also does not take into account future contributions that are to be received, growth that will take place on those contributions, or the future growth on the contributions already made.

19. The insurer concludes by stating that the investment return of R225 859.01 that was added to your total contributions translates to a rate of return of 12.59% *per annum* on the contributions that you paid in, which contributions would have only achieved a return of 8.5% had they been invested in the mainstream inflation index.

## DETERMINATION AND REASONS THEREFOR

### Technical points

20. 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 *Louw v Central Retirement Annuity Fund and Another* [2005] 5 BPLR 622 (PFA) at paragraphs [17] to [36] and the authorities referred to therein, I cannot uphold the contention that this matter constitutes “long-term insurance business” over which I have no jurisdiction.
21. Furthermore, Davis J (in whose judgment Le Grange AJ concurred) in *Central Retirement Annuity Fund v Adjudicator of Pension Funds & Others* [2005] 8 BPLR 655 (C) at page 660C (“the *de Beer* judgment”) 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 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.”
22. In so far as your complaint relates to the administration of the fund and/or the investment of its funds and alleges that you have suffered prejudice (in that you have been paid a lesser benefit than what you expected) in consequence of the maladministration of the fund, your grievance constitutes a complaint as defined (See *Louw* (cited above) at paragraphs [11] to [15]).
23. While your letter of complaint does not make the allegations as required in the Act in the precise terms as would otherwise have been expected of a lawyer (which I gather you are not), it is clear that you are unhappy about the reduction of your fund value without prior warning by reason only of your having retired prior to the originally selected retirement date. In the circumstances, it would be unduly formalistic to dismiss the complaint by reason solely of failure to allege in precise terms as required by the Act.

1. The Cape High Court in the *de Beer* judgment said the following in this regard (at 660E-G):

“Applicant’s contention regarding [the complainant’s] letter is based upon a very formalistic reading of the complaints procedure as provided for in the Act. On this reading, the letter generated by [the complainant] 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 this case between Sanlam and applicant”.

24. The technical points are therefore dismissed.

### The merits

#### Illustrative values and the discounting of the maturity value

25. The statement of benefits that was issued to you when you increased your contributions during 2001, as well as subsequent benefit statements, contain the following information under the section titled “Provisos and assumptions”:

“Information supplied in this statement is subject to the provisions of the policy. *The actual benefits afforded by this policy shall be determined by the actual bonus rates, cost recoveries and bases of calculation applicable from time to time* (emphasis supplied).

Future inflation will influence the purchasing power of benefits. The purchasing power of the policy benefits will depend on how the bonus rates fared in relation to the inflation rate.

The values given above include the additional benefits in respect of premiums paid in terms of PENSION BOOSTER.

Illustrative values in this statement are subject to the following and calculated on the assumption that:

- Sanlam’s most recent rates of reversionary and terminal bonuses will remain unchanged for the values at higher bonus rates.
- Sanlam’s most recent rates of reversionary and terminal bonuses will be reduced in accordance with a 3% drop in annual rates of return for the values at the lower bonus rates.
- The annual pension will be payable on a monthly basis, until death, but in any case for a minimum period of 10 years.
- Sanlam’s current pension rates will remain unchanged.
- The basis for the allocation of benefits will remain unchanged in respect of

premiums paid in terms of PENSION BOOSTER.

Illustrative values have been calculated in line with the benefit illustration agreement of the LOA at two different bonus rates. These bonus rates are influenced by expected inflation and investment returns, for example, lower expected levels of inflation therefore lower expected investment returns may result in lower bonus rates. *The illustrations are not predictions of actual benefits and are not guaranteed* (emphasis supplied)."

26. The illustrative maturity values that were furnished to you over the years were not a prediction of the actual benefits that you would receive at retirement, and were also based on the assumption that you would pay contributions until 1 September 2007. Furthermore it was clearly stated in the policy documents that the illustrative values are not guaranteed. Thus the insurer and the fund cannot be held to them.
27. When you terminated contributions in September 2004, the insurer had to calculate the actual value of your early retirement benefit as at that date. The cessation of contributions before the chosen retirement date means that the investment period is shortened and the bonuses proportionately reduced. The discounting of an expected maturity value to its value at the early retirement date can be likened to the practice, which is employed by some defined benefit funds, of applying a reduction factor to the benefit of a member who goes on early retirement. The percentage of the reduction in the benefit on early retirement is usually determined by calculating the number of months short of normal retirement age.
28. Thus, you cannot claim to be entitled to anything other than the discounted value of the sum assured and the bonuses already declared as at September 2004. I cannot find any grounds for setting aside the adjustment of R86 717.17.

#### The "market value adjustment factor"

29. A persistent refrain that sounds through all the submissions filed by the respondents regarding the "market value adjustment factor" is that it is aimed at ensuring that the remaining members are not prejudiced by the early leavers through the former having to pay the difference between the value of the sums assured and bonuses and the market value of the benefits of the early leavers. They further state that the adjustment is "calculated according to the rules that an insurer must have and must apply, and which must be approved by the statutory actuary..." The respondents further seek to rely on a clause in the policy document which states that upon the acceleration or delay of the retirement date, the various sums and provisions of the policy will be amended as determined by Sanlam. The principles discussed in *Mungal v Protector Preservation Fund and Others* PFA/KZN/2658/05/KM as regards market level adjustors apply with equal force on the issues arising in this case in this regard.

30. The fund (and any other service providers engaged by the fund to perform some of its duties) may only do what is set forth in the rules (see *Tek Corporation Provident Fund & Others v Lorentz* [2000] 3 BPLR 227 (SCA) at 239D). The rules of the fund do not provide for the application of a market value adjustment factor for retiring early. Although the clause in the policy provides that “*by so ‘n vervroeging of uitstel word die bedrae en bepalings van hierdie polis verander soos deur Sanlam bepaal*”, the clause is so lacking in clarity and detail that one cannot discern therefrom what the amendment of the various sums and provisions of the policy entails. It is also not clear on what basis and in terms of what method Sanlam will determine the amendment of the sums. In the result, the meaning of the clause cannot be stretched so as to accommodate the application of a market value adjustment factor.
31. Not only are the trustees of a fund required to act in accordance with the rules of the fund and the applicable legislation, but they 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(2) of the Act codifies the common law fiduciary duty owed by trustees to the beneficiaries on behalf of whom they hold trust assets. T
32. In this regard, the words of 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 660D-E, quoted in paragraph 21 above, are apposite.
33. 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.”
34. While the practice of discounting the projected retirement value to the current one at the early retirement date is a fair and acceptable one, in my view, the same cannot be said of the practice of removing a proportion of

the investment return from members who leave early on the basis only of actuarial practice not underpinned by rule or policy provisions to which either the fund or the member is alive.

35. Since neither the rules nor the policy document authorize the application of the market value adjustment factor, the insurer was not authorized to adjust your early retirement benefit down by an amount of R32 917.15.

### Relief

36. The order of this Tribunal is as follows:

- 36.1. The relief sought on the basis of illustrative values is dismissed.
- 36.2. It is hereby declared that the respondents were not entitled to apply the market value adjustment factor to determine the complainant's early retirement benefit.
- 36.3. Sanlam Life Insurance Limited ("the insurer") is directed to calculate the retirement benefit which the complainant would have received had the aforesaid reduction not been effected.
- 36.4. The insurer is ordered to pay to the complainant, or transfer to an institution of her choice permitted by the rules of the fund and applicable legislation, the amount in paragraph 33.2, within six weeks of the date of this ruling.
- 36.5. The respondents are further ordered to pay interest on the amount referred to in paragraph 33.3 at the rate of 15.5% per annum, calculated from 1 November 2004 to the date of payment or transfer.

**SIGNED IN CAPE TOWN ON THIS**

**DAY OF**

**2006**

Yours faithfully

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**VUYANI NGALWANA**  
**PENSION FUNDS ADJUDICATOR**