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Please quote our reference: PFA/GA/12876/2007

Re: DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT, 24 OF 1956 ("the Act") – NICHOLSON M ("the complainant") v CENTRAL RETIREMENT ANNUITY FUND ("the respondent")

1. Introduction

[1.1] This complaint concerns the calculation of values of a paid-up policy in the retirement annuity fund.

[1.2] The complaint was received by this office on 2 March 2007. A letter acknowledging receipt thereof was sent to the complainant on 27 March 2007. On the same date a letter was dispatched to the respondent giving it until 27 April 2007 to file its response to the complaint. A response was received from the respondent on 27 April 2007.

[1.3] After reviewing the written submissions, it is considered unnecessary to hold a hearing in this matter. The determination and reasons therefor appear below.

2. Factual Background

[2.1] The complainant commenced contributing to the respondent on a policy 15579452x2 which he intends to make paid-up. The policy contract commenced on 1 May 1996 and has a maturity date of May 2032.

[2.2] The complainant obtained a quotation from the respondent which reflected the values if the policy is made paid up. He acknowledges that there will be some penalties payable but questions the maturity value if he makes it paid up.

3. Complaint

[3.1] The complainant submitted that according to the quotation he requested from the respondent, the minimum maturity value on his policy should it be made paid-up would be reduced from R87 522.00 to R45 745.00.

[3.2] The complainant would like the respondent to explain where the difference between the two amounts will be utilized for.

[4. Responses

[4.1] This office received a response from P G Jonker, the Legal Advisor of Sanlam's Law Services Department ("the insurer").

Long Term Insurance Act

[4.2] P G Jonker gave a detailed explanation about the provisions of the Long-term Insurance Act 52 of 1998 ("the Long-term Insurance Act") and submitted that the primary purpose of the Long- term Insurance Act was to protect the consumers by ensuring that the acceptable long term insurance products are provided to them (product regulation), that these products are provided in the acceptable way (market conduct regulation) and that the provider of these products (the long term insurer) is and remains financially sound (prudential regulation).

[4.3] P G Jonker submitted further that because the long term insurers must have sound financial status at all times, their business is subjected to actuarial supervision. Further that the long term insurers are required by law to have statutory actuaries, whose duty is to safeguard the financial soundness of the insurer.

[4.4] P G Jonker supported his submissions by making reference to the following definitions in the Long-Term Insurance Act:

> ***"Long-term insurance business"***
> the business of providing or undertaking to provide **policy benefits** under **long-term policies;**

"Policy benefits"

one or more sums of money, services or other benefits, including an annuity;

Long-term policy"

an assistance policy, a disability policy, fund policy, health policy, **life policy or** sinking fund policy, or **a contract comprising a combination** of any of those policies; **and includes a contract whereby any such contract is varied;**

"Life policy"

a contract in terms of which a person, in return for a **premium,** undertakes to-

a) provide policy benefits upon, and exclusively as a result of a life event; or

b) pay an annuity for a period;

and includes a reinsurance policy in respect of such a contract;

"Premium"

the consideration given or to be given in return for an undertaking to provide policy benefits;

"Life event"

the event of the life of a person or an unborn--

a) having begun;

b) continuing;

c) having continued for a period; or

d) having ended;"

[4.5] P G Jonker submitted that as Sanlam Life undertook to provide the policy benefits upon as a result of events in return for a premium as defined in the Long Term Insurance Act, the policy becomes a life policy which is a long-term policy and as such, part of the long-term insurance business of the insurer.

[4.6] P G Jonker made reference to Section 34 of the Insurance Act 27 of 1943 ("the 1943 Act") and explained that same prohibited the insurer from providing policy benefits that were not in accordance with the table of the rates of premium which it ordinarily charges and which it ordinarily undertook to grant. Further that the said table should be approved by the insurer's statutory actuary and to be furnished to the insurance Registrar to ensure that the premiums are actuarially sound, thus safeguarding the financial soundness of the insurer and protecting the policy holders.

[4.7] P G Jonker averred that section 34 of the Act 1943 was replaced by section 42 of the Long term Insurance Act and quoted same as follows:

> "A long-term insurer shall not--
>
> a) enter into any particular kind of long-term policy unless the statutory actuary
> is satisfied that the premiums, **benefits and other values** thereof are actuarially sound;
>
> b) make a distinction between the premiums, benefits or other values of different long-term policies unless the statutory actuary is satisfied that the distinction is actuarially justified; or
>
> c) award a bonus or similar benefit to a policyholder unless the statutory actuary is satisfied that it is actuarially sound and that a surplus is available for that purpose.

[4.8] P G Jonker added that section 46 of the Long Term Insurance Act safeguards the financial soundness of the insurers, thereby protecting the policy holders. Further that the insurers must apply the actuarial rules as provided in the latter section and approved by the statutory actuary.

Detailed response

[4.9] P G Jonker submitted that the inception date of policy 15579452x2 was 1 May 1999 with the contractual maturity date of 1 May 2032. Further that the minimum maturity value is not a present value but a future value calculated from 232 based on the assumption that the contributions will be paid until that date and therefore the calculations are made taking into account that no contributions will be received between 2007 and 2032.

[4.10] P G Jonker submitted that most of the expenses with respect to the policies are incurred at the commencement of the policy or when the premiums are increased and are recovered by means of charges, which are charged over the term of the policy. Further that when the policy charges were calculated it was assumed that the contractual premium would be paid to the end of the policy term and that if the premiums are stopped now, the insurer will be unable to recover the costs from the future charges.

[4.11] P G Jonker stated that the insurer reduces benefits by charging a premium termination charge in order to recover the expense of doing an alteration to the policy, recover loss of future policy charges which are required to pay the initial expenses already incurred.

[4.12] P G Jonker submitted that the premium termination fee is not a penalty but an amount with which the benefits were reduced. Further that the policy stipulated that:

> "If a premium is not paid within a period of grace and the waiting period as indicated in the schedule has not yet expired, the policy offers no benefits. If the waiting period has already expired, the policy is converted into a paid-up policy with reduced benefits according to the practice of Sanlam"

5. Determination and reasons therefor

[5.1] An insurance policy is in essence an agreement between the policy holder and a long term insurance company in terms of which the latter is to provide a specified benefit at the dates of maturity provided that the agreed premiums are paid for the agreed premium paying term. This means that the policy holder or the complainant in this regard will only become entitled to the benefits disputed in the policy if she or he pays the agreed premiums for the agreed premium term.

[5.2] The respondent is correct in its submission that part of the premiums paid are used to recover the costs incidental to the administration of the policy as well as initial expenses incurred by the insurers in respect of the development of the policy product, the distribution and marketing thereof and establishment of the infrastructure required to properly underwrite and administer the policy. These costs which must be obviously recovered if the insurer is to remain financially sound are allocated to all the policies in a specific portfolio.

[5.3] Furthermore, the insurer and the respondent are not in the position to charge any fees which are not actuarially sound as same will amount to contravening the provisions of section 46 of the Long –Term Insurance Act.

[5.4] The policy contract also provides that if the contributions cease, the benefits will be reduced according to the practice of the insurer.

[5.5] In view of the above, the respondent and the insurer will be acting properly in terms of the rules of the respondent, the policy contract, the Act and the Long Term Insurance Act.

[6] Relief

[6.1] The complaint is dismissed.

DATED AT JOHANNESBURG ON THIS DAY OF 2008.

Yours faithfully

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MAMODUPI MOHLALA
PENSION FUNDS ADJUDICATOR