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Dear Sir,

DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT, 24 OF 1956 (“the Act”): J BARNARD (“complainant”) v SOUTH AFRICAN RETIREMENT ANNUITY FUND (“first respondent”) AND OLD MUTUAL LIFE ASSURANCE COMPANY (SOUTH AFRICA) LIMITED (“second respondent”)

[1] INTRODUCTION

- 1.1 The complaint concerns the quantum of the causal event charges imposed by the second respondent on the complainant’s fund value on making his policy paid-up and on transferring to another retirement annuity fund.
- 1.2 The complaint was received by this Tribunal from the Ombudsman for Long-Term Insurance on 10 February 2012. A letter acknowledging receipt thereof was sent to the complainant on 27 February 2012. On 28 February 2012, letters were sent to the respondents requesting responses to the complaint by no later than 6 April 2012. A response dated 8 March 2012 was received from the second respondent. On 4

The Office of the Pension Funds Adjudicator was established in terms of Section 30B of the Pension Funds Act, 24 of 1956. The service offered by the Pension Funds Adjudicator is free to members of the public.

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May 2012, a letter was sent to the complainant requesting a reply to the response by no later than 25 May 2012. No further submissions were received from the parties.

- 1.3 After reviewing the written submissions before this Tribunal, it is considered unnecessary to hold a hearing in this matter. This Tribunal's determination and its reasons therefor appear below.

[2] FACTUAL BACKGROUND

- 2.1 The complainant applied for and was admitted to the membership of the first respondent, which is a registered retirement annuity fund in terms of the Act, on 1 December 2001. A retirement annuity fund policy with no. 12900639 ("the policy") was issued to him. The premium payable in terms of the policy was R600.00 per month increasing annually with the Consumer Price Index. The second respondent is the underwriting insurer and administrator of the first respondent. The complainant advised the respondents of his wish to make the policy paid up in March 2006. The policy was made paid up on 9 March 2006 and a causal event charge in the amount of R7 346.85 (16%) was imposed on the complainant's fund value. The complainant's fund value immediately before his policy was paid-up was R43 377.98 ("pre-causal event fund value") and as a result of his decision his fund value decreased to R36 031.13 ("post-causal event fund value").
- 2.2 The proposed causal event charge to be imposed by the second respondent on the complainant's fund value was R6 427.08 (11.16%). The complainant's fund value immediately before his proposed transfer was R57 577.49 ("pre-causal event fund value") and as a result of his decision his fund value would decrease to R51 150.41 ("post-causal event fund value").
- 2.3 With effect from 1 December 2006 the Minister of Finance, in terms of section 72 read with section 54 of the Long-term Insurance Act, no. 52

of 1998 (“LTI Act”) amended the regulations under the LTI Act (“the regulations”) to make provision for maximum limits regarding the values and charges that may be imposed on retirement annuity fund policies. Pursuant thereto, the second respondent evaluated the adjusted pre- and post-causal event fund values and concluded that no adjustment was required because it fell within the permissible range stipulated in the regulations.

[3] COMPLAINT

3.1 The complainant is dissatisfied with the causal event charges imposed by the second respondent on the policy on making it paid-up and should he transfer his fund value to another retirement annuity fund and wants this Tribunal to investigate whether or not the causal event charges are excessive.

[4] RESPONSE

4.1 The respondents confirmed the facts summarised above. They state that the premiums payable under the policies are not solely utilised to provide the policy benefits. Part of the premiums are used to recover the costs associated with the administration of the policies over their term, to fund part of the initial expenses incurred by the second respondent in respect of the development of the policies’ product and to fund the distribution and marketing thereof and the establishment of the infrastructure required to properly underwrite and administer the policies. These costs which must obviously be recovered if the insurer is to remain financially sound, are allocated *pro rata* to all policies within a specific policy portfolio. These expenses are incurred upfront and are therefore fixed and applied to every policy irrespective of whether the policy ends prematurely or continues to operate until the contractual end date.

- 4.2 The expenses associated with the each policy are borne by the member or life assured of that policy. These expenses are not subsidised by other members of the first respondent. This principle ensures fairness between members and is fully supported by the legal framework within which such contracts are regulated. The LTI Act dictates that the causal event charge has to be calculated in accordance with generally accepted actuarial principles and practices. When determining benefit reductions the Statutory Actuary must have ensured that the rules are in place in accordance with which the benefit reduction is calculated.
- 4.3 It implements Market Value Adjusters to more accurately reflect the actual value of the underlying assets, especially when the market is low. The reason for this action is to ensure equity between on-going policyholders and members that withdraw funds prior to the contractual retirement date. The aim of the Market Value Adjusters is to protect the interest of those investors who remain in the first respondent. This has the effect of providing the true market value, rather than a smoothed market value, to those who choose to leave the first respondent. Early withdrawal from the first respondent could lead to losses being made in the policy's underlying investment funds. By adjusting early withdrawal values to more accurately reflect the actual value of the underlying assets, it is protecting the future benefits of on-going members of the first respondent. The Market Value Adjuster percentage depends on market performance. When markets deteriorate further or improve sufficiently, the adjuster percentages are reviewed and adjusted or removed. The Market Value Adjuster is not a charge and no product provider benefits from the introduction of Market Value Adjusters. The causal event charges imposed on making the policy paid-up and to be imposed on transferring to another retirement annuity fund are in terms of the regulations.

- 5.1 The complainant is dissatisfied with the quantum of the causal event charges imposed by the second respondent on the complainant's fund values on making the policy paid-up and should he transfer his fund value to another retirement annuity fund. This Tribunal needs to determine the reasonableness of the causal event charges imposed by the second respondent.
- 5.2 The basis for imposing causal event charges needs to be determined and it must be decided whether or not the causal event charges imposed by the second respondent are fair and reasonable. In this regard Fourie J, in *Old Mutual Life Assurance Company (SA) Ltd v Pension Funds Adjudicator and Others* [2007] 1 BPLR 117 (C) at paragraph 35, noted that:

"The fact that the policy does not specify a formula according to which the paid-up reduced benefit is to be calculated, does not mean that Applicant has an unfettered discretion to arbitrarily determine a value in a manner that is unfair, unreasonable or capricious. In this regard, I am in agreement with Applicant's submission that the provisions of the LTIA, referred to hereunder, dictate that the paid-up reduced benefit to which Second Respondent is entitled has to be calculated in accordance with generally accepted actuarial principles and practice."

- 5.3 With the learned judge having confirmed that causal event charges may be imposed by underwriting insurers, what remains is to ascertain the fairness and reasonableness of the proposed causal event charge. This Tribunal takes cognisance, firstly, of the provisions of section 46 of the LTI Act, which reads 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 policy-holder unless the statutory actuary is satisfied that it is actuarially sound and that a surplus is available for that purpose.”

- 5.4 Further, section 52 of the LTI Act prescribes the manner in which long-term policies are to be dealt with in the event of premature cessation of contributions. The insurer must have rules approved by the statutory actuary that prescribe a sound actuarial basis and the method to be used to value a long-term policy in the event of a causal event occurring. Thus, the benefits and values attaching to a prematurely terminated policy, and any distinctions between it and policies that do not prematurely terminate, must be actuarially sound.
- 5.5 Lastly, in addition to the requirement that causal event charges must be computed using generally accepted actuarial principles that ensure the actuarial soundness of the insurer, on 1 December 2006 the Minister of Finance promulgated regulations in terms of the LTI Act that stipulate maximum causal event charges in respect of causal events that occurred on or after 1 January 2001.
- 5.6 This Tribunal requested an independent actuary to review the causal event charges imposed on the complainant's investment values. He found that the charge of R7 346.85 (16%) and the proposed charge of R6 427.08 (11.16%) in respect of the policy were fair and reasonable and in line with the regulations. The causal event charges were within the parameters in the regulations.
- 5.7 After careful consideration of the facts placed before this Tribunal it is evident that the second respondent acted in accordance with generally accepted actuarial practice, the provisions of the rules, the provisions of the policy documents, the provisions of the LTI Act and the regulations. This Tribunal accordingly finds that the submissions do not

support the complainant's submission that the causal event charges are unfair, unreasonable or capricious in nature.

[6] ORDER

1. In the result, the complaint is dismissed.

DATED AT JOHANNESBURG ON THIS 1ST DAY OF AUGUST 2012

MA LUKHAIMANE
DEPUTY PENSION FUNDS ADJUDICATOR

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