

PERSONAL FINANCE

Life assurer deducts penalties twice

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A life assurance company may impose a penalty when you reduce the premium on an investment policy and again when you stop paying the premium completely.

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A couple in their late 60s with a huge shortfall in their retirement capital have recovered more than R62 000 in confiscatory penalties that were deducted from policies with 15-year investment terms.

Old Mutual refunded almost R41 000 of the penalties when the financial advice ombud asked the life assurer whether the couple had been double-charged.

Noluntu Bam, Ombud for Financial Services Providers, ordered the company that employed the broker who sold the policies to make good for another R18 000. The company had repaid some R3 500 before the couple complained to the ombud.

This is the third time this year that either the financial advice ombud or the Pension Funds Adjudicator, Muvhango Lukhaimane, has queried the application of early termination penalties and, as a result of their queries, the life assurance companies concerned have reduced the penalties.

Life companies impose the penalties when you reduce or stop paying your premiums on a retirement annuity (RA) policy or your contributions to an endowment policy, or when you withdraw your savings from an endowment policy before the policy matures. The life companies refer to these actions on your part as “causal events”.

There are limits on the penalties that the life insurers can impose, and the Financial Services Board (FSB) is seeking to ensure that the penalties are not imposed unfairly when you alter your RA or endowment contract more than once.

However, until the FSB's measures are in place, you would do well to question penalties that are imposed more than once (see "Penalties may be levied more than once by mistake", below).

According to Bam's ruling, Mr and Mrs V, of Springs in Gauteng, were 69 and 66 years old respectively when, in early 2008, Charlene van Niekerk, a representative of Kampstone Financial Services, sold each of them a Max Investment Committed Plan with a 15-year term. The policies had recurring monthly premiums of R2 000 and R5 000.

Mrs and Mrs V said they told Van Niekerk they wanted to invest for two years and wished to have unrestricted access to their capital if an emergency arose.

They complained that, at their advanced age, they should not have been sold policies with such long terms, and they incurred the penalties when, because they could no longer afford the premiums, they had reduced the premiums and then prematurely cancelled the policies.

The couple said the penalties were not disclosed to them when they took out the policies.

Bam's ruling notes the contents of the record of advice given to Mr and Mrs V, which Kampstone provided to her office. It states that Mr and Mrs V had insufficient retirement capital and wanted to save for retirement on a monthly basis as a matter of urgency.

"There is a huge capital shortage," the record of advice notes.

Gerda Dafel is the sole member and key individual of Kampstone. (A key individual is responsible for managing the financial services provided by an entity and overseeing the services provided by the entity's representatives.)

When asked by Bam to respond to the complaint, Dafel told the ombud that Van Niekerk had offered Mr and Mrs V a money market investment and a "four-year" RA. The couple had rejected the money market investment, because it paid too little interest, and the RA, because the term was too short.

According to Dafel, the couple chose the Old Mutual investment policies and assured Van Niekerk that the premiums were affordable.

Mrs V signed a record of advice that stated she understood the consequences of disinvestment, cancellation and a reduction in the premium, Dafel told Bam.

The record of advice that Mrs V signed states that "costs are applicable in the event that the contract is stopped before the term has ended".

In October 2008, the couple made the first of nine withdrawals from the two policies and were incurring penalty charges.

By the time Mr and Mrs V made both policies paid-up (stopped paying the premiums altogether) two years later, the penalties amounted to R46 370 and R16 367 respectively.

Bam asked Old Mutual to confirm that the penalties were correct and to clarify what charges were levied for the partial withdrawals and for making the policies paid-up.

The ombud's office concluded that Mr and Mrs V had been double-charged – a practice known as double-dipping – for multiple "causal events". A common example of double-dipping is where a life

company charges a penalty when you reduce the premium and again when you make the policy paid-up.

Old Mutual subsequently reduced the penalties by R30 827 on one of the policies and R10 183 on the other.

Financial advisers are obliged in terms of the Financial Advisory and Intermediary Services (FAIS) Act to consider financial products that are appropriate for your needs.

Bam found the record of advice did not contain a comprehensive list of all the products that Van Niekerk considered suitable for Mr and Mrs V. The record also did not contain an explanation of why the Old Mutual policies were likely to satisfy Mr and Mrs V's needs and objectives, she says.

"I do not accept that the information provided to the complainants was adequate in the circumstances to place them in a position to make an informed decision. Given the fact that the potential penalties payable on the products were such a material consideration, [Kampstone] was duty-bound to make full and frank disclosure," she says.

The record of advice is the only document that "alludes" to the early termination penalties, Bam says.

The same document is "silent on the investment term of the contracts, which has a direct correlation to the severity of the penalties payable should the contracts be prematurely cancelled", she says.

The policies were due to mature after Mr and Mrs V's expected life-spans as predicted in mortality tables drawn up by actuaries for the life assurance industry.

Bam noted that there was no proof that the commission earned by Van Niekerk was disclosed to Mr and Mrs V, and this commission was linked to the term of the policies.

Van Niekerk "merely paid lip service to the provisions of the [FAIS] Act and the code [of conduct under the Act] to create an illusion of compliance", Bam says.

The ombud also noted that Dafel had had concerns about Van Niekerk's conduct in her dealings with Mr and Mrs V, but Dafel had not had adequate measures in place to eliminate, as far as possible, the risk that her clients could suffer financial loss as a result of her representative's misconduct.

Bam found that Van Niekerk's actions caused Mrs and Mrs V to incur a financial loss, which were the penalties, less the refunds from Old Mutual and the R3 500 that Kampstone paid to Mr and Mrs V.

The ombud ruled that the loss amounted to R12 042 on one policy and R6 203 on the other. She ordered Kampstone and Dafel to repay these amounts to the couple.

PENALTIES MAY BE LEVIED MORE THAN ONCE BY MISTAKE

If penalties are applied to your retirement annuity (RA) or endowment policy more than once, query them, because they may well have been levied by mistake.

When asked about the huge reduction in the penalties that were applied to the policies of Mr and Mrs V, who recently took their case to the Ombud for Financial Services Providers Noluntu Bam, Old Mutual's general manager, Adrian Burke, said the company's administration systems are "not

automated in respect of multiple causal event charges". As a result, he says, it "is unfortunately possible for errors to occur".

A "causal event" is where you alter the terms of your RA or endowment policy, such as by reducing or stopping your contributions or transferring the policy proceeds before the end of the contract term.

Burke says that whenever Old Mutual becomes aware of the "occasional cases" where the fund value is reduced by more than the maximum amount that life insurers can charge, it limits the multiple causal event charge. This was what happened in the case of Mr and Mrs V, and they were refunded the incorrectly applied penalties, he says.

The Financial Services Board (FSB) recently issued a draft directive aimed at providing greater clarity on how life insurers should apply penalties where multiple "causal events" occur, he says.

The FSB's intervention followed a complaint that was lodged with Bam in May and one that was submitted to Pension Funds Adjudicator Muvhango Lukhaimane in June.

In the case that went before Bam, Momentum discovered it had made an R800 000 mistake in the penalties it levied on the policies of two brothers. The brothers had wanted to invest lump sums of R1.2 million and R1.5 million in an endowment policy, but their adviser had drawn up a contract indicating they would invest these amounts annually for 10 years.

When the brothers discovered the fraud, Momentum imposed penalties of more than R1 million, which were reduced only when the brothers complained to Bam.

In the case that went before Lukhaimane, Momentum agreed to reduce, by R38 386, a penalty of R172 095 that it imposed on the savings of a member of the Momentum Retirement Annuity Fund after four "causal events".

Lukhaimane checked Momentum's calculations with an independent actuary, who found that the reduced penalty was "excessive" and reduced it by a further R10 390.

Burke says that Old Mutual and other life insurers provided input for the FSB's draft directive.

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