



RETIREMENT PLANS - WHAT CAN GO WRONG: THE 'TWO-THIRDS' RULE

When we retire from a pension or retirement annuity fund, we are compelled by law to leave two-thirds of our retirement savings in order to purchase an annuity or an annual income, which can be paid on a monthly or quarterly basis.

There are a number of options available as to the type of annuity we can buy with that 'two-thirds'. What must be clear though is that the two-thirds cannot by law be accessed by way of a lump sum. What we do with the one-third is up to the individual but it is the only portion of our retirement savings that can be available by way of a lump sum.

We have recently noticed a spike in complaints involving annuities. Complainants - and they come from all over the country - say that they were not made aware that they cannot 'withdraw' further lump sums from the remaining two-thirds of their retirement savings, after they had purchased the annuity.

In most of these cases, the complainants had already accessed the one-third portion.

Here are some case studies which illustrate some of the pitfalls when people try to access their retirement funds.

Mr V versus Provider

Two years after purchasing a life annuity with the insurer with the capital amount of R 503 000, Mr V made several attempts to withdraw a further lump sum from the remaining two thirds of his retirement savings because he needed the money to pay certain things. The insurer kept to the same line of explanation that it was not possible to make the 'withdrawal'. The law simply did not allow it.

A complaint was eventually lodged with the FAIS Ombud.

In his complaint, the complainant stated that prior to purchasing the annuity, he had made the plea to the provider that he would like to have access to his funds as and when the need arose. The response by the provider allegedly was that the complainant could still access the funds at any time. All the complainant needed was to write to the insurer and request the amount they needed.

Our intervention:

We could not help the complainant. Although we had several questions to raise with the provider, there were practical difficulties, based on the complainant's circumstances, that made it hard to question the appropriateness of the advice.

Lessons:

- We find that complainants are not aware that upon contracting with the insurer to purchase a life annuity, the capital ceases to exist and is replaced by an obligation on the part of the insurer (provider), to pay the annuity until the end of the annuitant's life.
- We find that complainants believe that they could 'withdraw' from their capital at any time.
- Notwithstanding the questions concerning the quality of the records of the providers involved, we find it difficult to criticize the advice on the basis of appropriateness.

VEHICLE INSURANCE: RISKS INVOLVED IN NOT CORRECTLY IDENTIFYING THE REGULAR DRIVER¹

The case of 'Mrs M'

Mrs M, the premium payer and policy holder, contacted her insurer to change the regular driver on her policy from her deceased husband to her son. The change made by Mrs M resulted in her initial premium amount of R627.07 being increased to R1 737.39 due to her son's risk profile. Mrs M decided to cancel her policy. However, when she met with another provider, Mrs M alleges she was advised to mention that she was the regular driver in order to keep the premiums low. Mrs M considered the lower premium as a better deal and accordingly allowed the representative to record in the proposal form that she was indeed the regular driver. The vehicle was later involved in an accident and Mrs M lodged a claim. The claim was rejected due to the incorrect information that was furnished at proposal stage. The insurer argued that it had been prejudiced as a result of the incorrect information that was furnished. Despite having named herself the regular driver, it was uncovered that her son drove the vehicle on a regular basis and in fact was the driver at the time of the accident.

A complaint was eventually lodged with the FAIS Ombud.

Our intervention:

We raised several questions relating to advice on the part of the representative. The representative acknowledged their failure to disclose the consequences of making Mrs M the regular driver of the vehicle. Taking into account the circumstances of the complainant, the insurer agreed to resolve the matter by paying a portion of the claim. A certain amount was withheld as the insurer argued that it had been prejudiced as a result of the representation that Mrs M was the regular driver.

Lessons:

- It does not help to save on the premium only to receive an unpleasant surprise when the truth is uncovered.
- The correct identification of the regular driver is not a matter between you and your broker. It is a matter that the insurer needs to know to properly assess risk.

INVESTMENTS: IF IT IS TOO GOOD TO BE TRUE ...

There does not seem to be an end to the number of street-smart jokers who go around selling investments with ridiculous promises of 40% to 50% returns over three, six or twelve months. What is strikingly odd is that people believe them. Professional people are also not immune to these fraudsters.

There are currently a large number of complaints relating to investments made on the basis of exotic returns. We find that people have not taken the time to properly investigate the investments. They consider their circumstances and are so attracted by the promise of riches in the event the transaction is successful that they put their money down too quickly.

The case of the attorney

We single out a complaint that was lodged by a practising attorney who complained that she made an investment of R600 000 based

on the promise of a return of 50% over a period of six months, after speaking to a gentleman who claimed all sorts of successes with investments including being a specialist in the import/export market.

Without verifying the claims, complainant made the investment exactly one week later. The funds were deposited into the bank account of an entity, which was later liquidated. The complainant was unaware of the liquidation.

At the end of six months, she telephoned and wrote letters to the respondents for the repayment of the capital and interest. Not only was the respondent in default of paying the interest, there was no chance of recovering complainant's capital.

The respondent retorted that he never gave any advice in terms of the FAIS Act and promptly pointed to the fact that the entity into which complainant's funds went no longer exists. Although the respondent finally conceded to giving advice, his estate was also sequestrated prior to the completion of our investigation. The Office later learnt from the complainant that he had vanished.

Our intervention: We advised the complainant to seek legal advice with regard to the possibility of lodging a claim with the liquidator of the entity into which her funds went into. In the end, we could not help the complainant.

Lessons:

- There should be no pressure involved in investing. It does not matter that the offer may expire a day later or in a matter of hours. If the provider or the person introducing the investment pressures you to rush so that you make it before the expiry of the offer, let it pass you. You will soon thank yourself.
- If the provider is not forthcoming with details of who owns the business and other pertinent details, such as the people who are responsible for the running of the business, rather pass on the offer.
- If you are not allowed sufficient time to make enquiries with the necessary authorities, including people in your family, friends and associates, pass on that offer.
- If there are no clear details or the explanation of what generates the seemingly impressive return sounds even slightly complicated, pass, you will soon realise why it was not for you.
- If you and/or none of your family, friends or associates have ever heard of the company, then do a lot of investigative work before you part with your hard earned money.
- Ask yourself this question: if the returns promised were realistic, would there be any need for the person talking to you to do so? The answer most certainly should be no.
- Do not be persuaded by statements to the effect that the introducer of the investment has, or his family and friends have, invested with the same company. That may or may not be the case but it still does not mean the investment is suitable for you.
- Remember the old age adage, 'a fool and his money are soon parted.'

¹ Is the person who drives the insured vehicle most often and more frequently than any other person, and may not necessarily be the insured. (<http://www.hippo.co.za/insurance-glossary>)

FIXED TERM INVESTMENTS AND YOUR LIQUIDITY NEEDS

The case of END v Provider

The complainant invested R100 000 for a period of 5 years with an insurer. Within a year, she had made a loan and a partial surrender. When she sought further access to her funds, she was told she could not, much to her surprise.

The insurer pointed to the provisions of section 54 of the Long Term Insurance Act, which regulate fixed term investments.

Our intervention:

We requested proof that the advice offered to the complainant was suitable to her financial circumstances at the time of rendering advice. The insurer wrote back offering to resolve the matter with the complainant by way of an offer, which complainant accepted.

Lessons

- In addition to all the other pertinent questions when you invest, there must be questions that deal with your liquidity needs. For example, your provider must ask, “When are you going to need the money?” and/or “Do you have any money that could be readily available in the event of emergency?” These are questions you must discuss with your financial advisor. If these are not asked, you may be heading for an unpleasant surprise.
- If the financial advisor rushes you through the sale to sign the proposal forms before you are asked for details of your financial circumstances, you must know the advice may not be appropriate for you.
- If you do not give details of your financial circumstances to your financial advisor, the advice may not be appropriate.
- Details of your financial circumstances are required so that the provider can provide you with financial advice that suits your financial needs.

FUNERAL POLICIES: STRANGER’S DEATH, A JACKPOT

A funeral policy is a policy taken out on one’s life in order to assist the family with the costs of sending away a loved one with dignity.

Funeral policies taken out on strangers’ or distant family members are becoming a phenomenon among many people and this is evident from the complaints this Office deals with.

Whilst there is no gainsaying the moral obligation that people place on themselves to bury family with dignity, there is widespread evidence of abuse of the system of funeral insurance. Owing to the rising number of these types of complaints, we have been able to identify trends and one such trend points to the lack of insurable interest in many cases.

While we as an office are under no illusion about the difficulties relating to this area of business and the manner in which financial services are rendered based on, amongst others, the levels of sophistication, the vulnerability that is consequential from latter, the lack of record keeping and more, there is clearly cause for concern.

We also appreciate that in many instances, the funeral policy may be the only financial arrangement the complainant may have ever engaged in.

The case of Mr D

The case involving Mr D is one such case. Mr D complained to our office that the scheme administrators had refused payment on a claim he had lodged for funeral costs, following the death of his wife.

After visiting the offices of the funeral scheme several times, he was told there would be no payment made and this was provided in writing, albeit in somewhat confusing manner.

A complaint was eventually lodged with the FAIS Ombud. Mr D had provided proof of payment of the premiums (by way of bank statements) together with copies of the original documents, which confirmed cover. The complaint was referred to the funeral scheme administrators who promptly provided a reply. Their version was tested with the complainant who replied with a terse statement challenging the version of the respondent.

Our Office decided to telephone the complainant to clarify a number of areas that had been raised by the respondent, which complainant had not address in his response.

Firstly, the mobile number turned out to be that of a woman, who had no knowledge of the complaint including indicating that the deceased was not related in any way to her family. Further investigation led us to a woman who provided proof that the name used in the complaint was that of her retired father, who, prior to reaching his retirement age had not been employed for over twenty years. She clearly indicated that her father had no mobile phone, no income out of which he could service premiums for a policy and was in all probability not the one who had taken out the policy or even lodged the complaint. What made the case more bizarre is the fact that the woman told our office that her mother died more than fifteen years ago.

We dismissed the complaint as there was no complainant. The case was clearly heading towards a criminal investigation which this office is not empowered to handle.

CLAIMS OF BLOOD RELATIONSHIP BY A FINANCIAL ADVISOR

The case of Ms B

Fairly recently we received a complaint from a particular Ms B, alleging that a broker, Mr D, who had assisted her to take out a funeral cover over her niece’s life had done a double take, in that he too applied for funeral cover over the life of the same person. In so doing, the broker had simply used the information he obtained from the complainant.

Since Mr D was well acquainted with the complainant’s family, when the niece eventually passed away, Mr D phoned the complainant’s sister and informed her that a representative from his workplace would phone her. He added, the sister should lie and say that he (Mr D) is related to the deceased.

In any event, following the lodgement of the claim for benefits, the complainant's claim was paid. After the funeral the complainant approached Mr D's manager to address the issue, who - as unreal as this sounds - allegedly suggested that the complainant be paid "for her silence".

Although the complainant's claim had been paid, she nevertheless complained to our office as she found the entire circumstances bizarre. Clearly, the complainant thought, she may be too late to stop the payment. The least she could do was to lodge a complaint with the FAIS Ombud.

Our intervention:

The matter was referred to the regulator.

Lessons:

As much as financial advisors are expected to act honestly in terms of the Code, not every financial advisor does.

TAX IMPLICATIONS AND RETIREMENT ANNUITIES

You have to ask your financial advisor to explain the meaning of tax relief before investing into a Retirement Annuity. Understand that tax relief may mean different things to different people. As an incentive the government gives tax relief to people who make contributions to retirement annuity funds. There is a strict formula that your financial advisor must explain to you. There are other important means of protection that the law affords you whilst your money is in a retirement annuity.

It does not mean that right from the day you start, monthly, after paying your premiums, the government will put that premium back into your salary. Nor does it mean that monthly after paying your premium, the tax you paid the previous month will reduce by the total amount of the premium.

A retirement annuity is a savings plan to make provision for your retirement. Money that is paid into a retirement annuity is locked in until the age of 55, being the earliest date you can retire from a retirement annuity fund. You can choose a later date and your financial advisor must explain what that means.

Case 1

The complainant is a school teacher who was advised to take out two retirement annuity contracts. She states in her complaint that she was advised that she was paying too much tax and in order to fully counter same, she needed the two contracts. She eventually found out that this was not the case. She then demanded repayment of her premiums from the insurer, which the insurer could not do.

The complainant sought our intervention.

Our intervention: We pointed out to the complainant that by law she would not be able to access her premiums until she retires on the date stipulated in the contracts or the early age of 55.

Be aware that the tax free portion at retirement is not cast in stone

Your tax free portion at retirement is not cast in stone. In other words, it is influenced by the withdrawals you made during your working life.

As the FAIS Ombud we recognise that much is required from Financial Services Providers when rendering financial services to a client. They are often required to seek relevant information that will enable them to advise clients accordingly. The case of Mr B and his trusted advisor/broker, which is set out below, speaks clearly to this requirement of relevant information being essential to providing appropriate advice.

Case 2

Mr B met with his advisor wanting to withdraw R600 000.00 from his Provident Fund. He was informed that he could access R315 000 tax free and of the remaining R285 000 only R36 000 would be taxed. However, SARS deducted R216 059 as tax. Infuriated by what appeared to be the incompetence on the part of the provider, Mr B lodged a complaint alleging that his provider had failed to inform him of the tax implications applicable at the time the financial service was rendered.

Our intervention:

According to the correspondence received, the provider stated Mr B had failed to disclose he had utilised his tax free benefit prior to consulting with him. However, Mr B was certain he had informed the advisor he had taken a retrenchment package before and requested that all his funds be paid out in full.

To decide on the differing version of events our Office required compliance documents from the provider detailing the information sought from Mr B prior to providing advice. It became clear that Mr B had disclosed having taken his retrenchment package at the time the financial service was rendered.

We decided that although the provider was not a tax practitioner, he ought to have known of the tax implications, given the information furnished by complainant. At the very least, Mr B should have sought assistance from the appropriate authorities.

An offer of R100 000 was made to Mr B and the matter settled.

Lessons

- Relevant information should be sought prior to providing financial services to clients.
- Limitations on the part of the provider should be clearly conveyed to clients
- Tax implications relating to withdrawal of lump sums at retirement should be discussed and verified from SARS
- All matters are decided on based on the documentary evidence provided.



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