

**2004 Pension Lawyers Association Conference**  
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**CHANGING TOMORROW**  
**SHARING KNOWLEDGE AND EXPERIENCE.**  
**PREPARING FOR THE FUTURE.**

**Topic: LIVING ANNUITIES: LEGAL ISSUES**

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**Organisation: Old Mutual**

# LIVING ANNUITIES: LEGAL ISSUES

Rosemary Lightbody

# Living Annuities

- Legal status
- Structure
- Applicable legislation
- Legal issues

## Legal Status:

### Is a “living annuity” an annuity?

- Case law - The distinction between an annuity and an installment payment is that an annuity involves an exchange of capital for income.
- Living annuities first developed over 10 years ago – doubt as to whether they constituted annuities or not.
- Balance of capital being available on death does not fit the conventional definition.
- SARS RF1/96 Aug 1996 – flexible annuities recognised by Revenue as annuities, subject to certain parameters (5/20%; annual review).

# Structure

- Provided by pension fund, or
- Purchased from insurer in fund's name, or
- Purchased from insurer in annuitant's name.

# Applicable legislation

- Pension Funds Act
  - s 37 A, B, C?
  - Investment Regulations?
  - PF 78; PF 100
- Long-term Insurance Act
  - s 37
  - s 63
  - Policyholder Protection Rules
  - Investment Regulations?
  - Directive 135 & 135A

# Applicable legislation (cont.)

- Income Tax Act
  - Definitions
  - Second & Fourth Schedules
  - RF1/96
  - GN 18 & 18A
  - GN 16
  - GN 19
- LOA
  - LOA Code on Flexible annuities

# Legal issues

- Does pension fund's liability cease where annuity is issued in the member's name?
- Does s37C apply?
- Directives 135 & 135A
- Living annuities issued to beneficiaries after death of original annuitant.



# 1. Does pension fund's liability cease where annuity is issued in the member's name?

- Theory: Once the annuity is purchased, the fund's liability passes to the insurer, and the annuitant ceases to be a member of the fund.
- PF 100 says that fund rules must state that membership of the of the fund shall cease on purchase of an annuity, and the fund will have no further obligation towards the member. However, last par acknowledges that there is uncertainty whether fund will in practice be relieved of all liability to the member. A court may decide otherwise.

# 1. Does pension fund's liability cease where annuity is issued in the member's name? (cont.)

- SARS GN 18 (August 1996)
  - Allows retirement funds to purchase an annuity from a S. African insurer in the name and on the life of a member who is retiring from employment.
  - Fund rules must provide for this, for the annuity to be compulsory, non-commutable, payable for and based on the life of the retiring member; and for the principles of 37A & B Pension Funds Act to apply.
  - Fund rules must provide for the transfer of liability to the insurer.

## 2. Does s37C Pension Funds Act apply?

- s37C directs the payment of “...any benefit payable by ...a fund upon the death of a member...”
- If the fund’s liability in respect of the annuitant no longer exists, then the annuitant is not a member, and so s37C does not apply.
- However, possibility of contractual inclusion.

# 3. Directives 135 & 135A

- S37 Long-term Insurance Act
  - S37(1): No transfer of any part of the business of a Long-term insurer shall have legal force without Court approval.
  - S37(2): An arrangement between insurers where the liability of one towards policyholders is substituted for that of the other, is deemed to be a transfer per ss(1) unless “the registrar is satisfied” that the policyholder is aware of the nature of the substitution and has agreed in writing.

## 3. Directives 135 & 135A (cont)

- Directive 135

Standing approval is granted for the replacement of a living annuity issued by an insurer with a living annuity or conventional annuity issued by another insurer.

Subject to conditions, one of which is the entering into a written agreement between the two insurers.

# 3. Directives 135 & 135A (cont)

- Directive 135A

Registrar considers it an undesirable practice for an insurer to refuse to transfer to insurer of policyholder's choice.

- Issues

- PF 100: Fund rules may provide for the insurer from which annuity may be purchased.
- RF1/96 requires living annuities to be reviewed annually to calculate minimum & maximum annuity benefits payable.

### 3. Directives 135 & 135A (cont)

- Where original annuity has s37C applicable, must transferee insurer's contract provide likewise?
- What is the effect of Registrar considering the refusal to transfer “an undesirable practice”?  
S50 Long-term Insurance Act.

## 4. Living annuity issued to beneficiaries after death of original annuitant – is this a “voluntary” annuity?

- **Taxation**

- **Does 2<sup>nd</sup> Schedule apply to lump sums?**

Definition of lump sum benefit includes any commutation amount payable “in consequence of *membership* or *past membership* of any fund”.

- **On death, may the annuity be commuted? Do definitions in s1 Income Tax Act apply?**

Definitions of pension fund & retirement annuity refer to *rules of the fund* providing for commutation. (6months after death of a member; one third only in case of RA fund).



## 4. Living annuity issued to beneficiaries after death of original annuitant – is this a “voluntary” annuity? (cont)

- GN 18 & RF 1/96

Applicable? Paying out over 5 years – 5/20% rule

- s37A & B Pension Funds Act

Both sections include an annuity purchased by the *fund* from an insurer for a *member*.

- s63 Long-term Insurance Act

Applicable.

## 4. Living annuity issued to beneficiaries after death of original annuitant – is this a “voluntary” annuity? (cont)

- Conclusion

Depends on the structure of the initial policy contract.

In many instances, the “pension” connection has been lost.

- Implications

- Pension Funds Act protection is lost
- SARS GN 18 restrictions do not apply
- Is it an annuity?