

## The suitability test: Long-term insurance



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The slow but tenacious  
wheels of justice



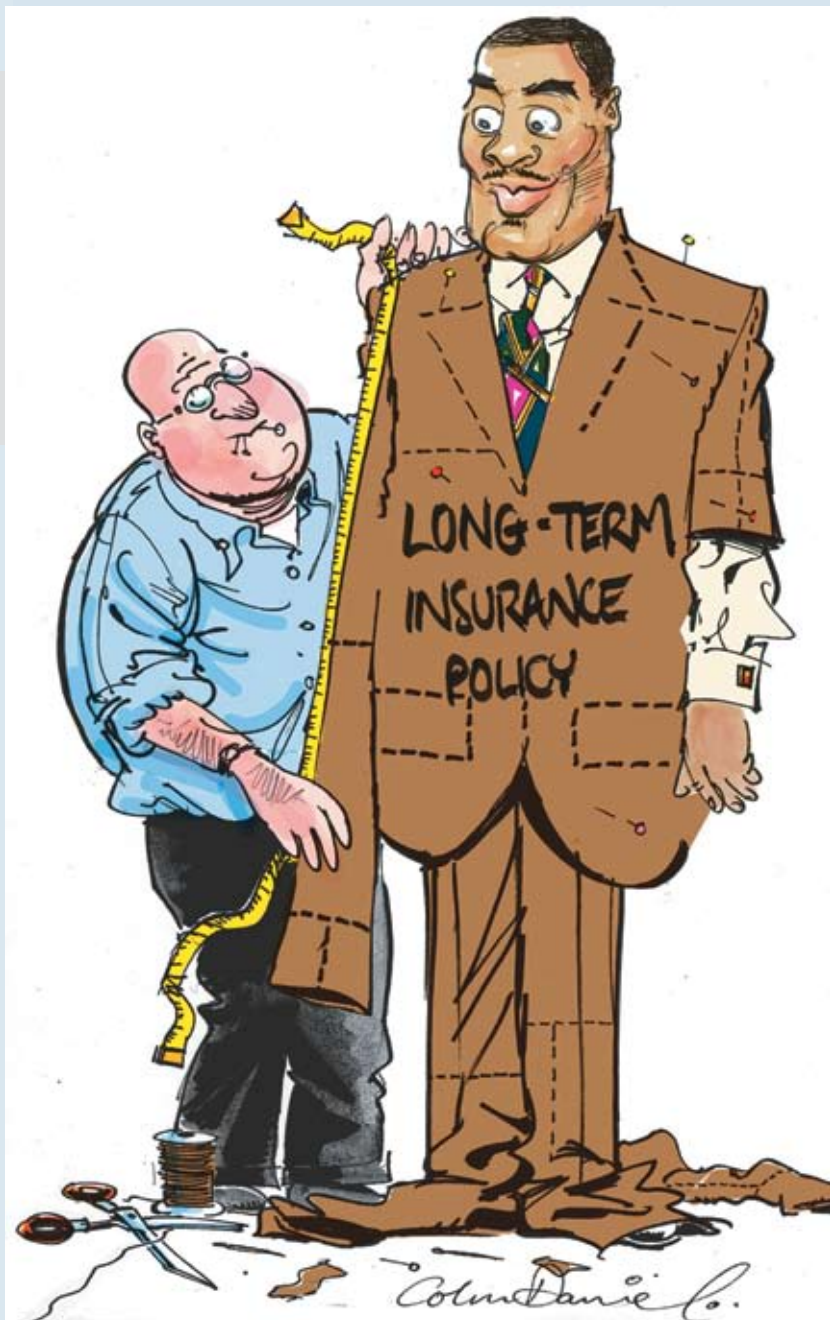
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Save us from the  
cost of death



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Consumer education  
finding its feet



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## EDITOR

Dr Franso van Zyl

## SUB-EDITOR

Bessie Venter

## EDITORIAL COMMITTEE

Russel Michaels  
Olivia Davids

## COVER AND GRAPHICS

IE Communications  
(012) 347 2882

## CARTOONS

Colin Daniel, *Personal Finance*,  
Independent Newspapers

## LAY-OUT

Greenpepper Communication  
Consultants (012) 332 1589

## SUBSCRIPTIONS

All subscriptions enquiries should be directed to Eunice Shikalange at the contact details below.

## CONTRIBUTIONS

Contributions to the FSB Bulletin are welcome and should be sent to the sub-editor at the address below. The editor reserves the right to edit contributions.

## POSTAL INFORMATION

PO Box 35655  
Menlo Park  
0102  
Republic of South Africa  
Tel: (012) 428 8155  
Fax: (012) 347 0669  
e-mail: eunices@fsb.co.za

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[www.fsb.co.za](http://www.fsb.co.za)

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## Change of address:

# New offices for the FSB

**“The FSB has settled into its new offices and it is business as usual”, says Russel Michaels, head of Communication and Liaison at the FSB.**

Michaels says the move to new premises has been necessary because of the FSB’s growth over the past 18 years. “The Board has reached saturation point, growing to 400 employees, who had to be accommodated in six buildings at the Rigel Park Offices in Waterkloof and Kasteel Park, in Erasmusrand. The move will co-locate the FSB staff at one office block. This will ensure ease of access by all FSB stakeholders to the Board,” Michaels says.

The new offices are situated at

Riverwalk Office Park, 41 Matroosberg Road, Ashlea Gardens. (See directions below.)

The move took place between 22 and 28 September. “Services were disrupted during this period but all services are now up and running. We appreciate our stakeholders’ patience during this period,” Michaels says.

### Directions

#### *From Johannesburg N1*

- Follow the N1 North (Ben Schoeman), direction Pietersburg(Polokwane).
- Pass Rigel off ramp (old FSB).
- Continue on the N1 toward Polokwane.
- Take the New Garsfontein off ramp.
- Turn left into Garsfontein Road.
- Turn right into Matroosberg Road.

- Look for Riverwalk Office Park on your right hand side.
- Enter the boom gates.
- The FSB is in Block B.

#### *From Polokwane*

- Follow the N1 south towards Johannesburg.
- Take the Atterbury off ramp.
- Turn left into Atterbury.
- Turn right into Lois Avenue also spelt Louis.
- Land mark - Menlyn Park Shopping Centre will be on your right hand side.
- Turn right into Garsfontein road.
- Turn right into Matroosberg Road.
- Look for Riverwalk Office Park on your right hand side.
- Enter the boom gates.
- The FSB is in Block B.

# The suitability test: Long-term insurance

By Anton Swanepoel, counsellor on FAIS

This article focuses on the requirements for long-term insurance products in terms of paragraph 8(1)(a), (b) and (c) of the General Code of Conduct, which states:

*A provider... must, prior to providing a client with advice-*

*(a) take reasonable steps to seek from the client appropriate and available information regarding the client's financial situation, financial product experience and objectives to enable the provider to provide the client with appropriate advice;*

*(b) conduct an analysis, for purposes of the advice, based on the information obtained;*

*(c) identify the financial product or products that will be **appropriate** to the client's **risk profile and financial needs**, subject to the limitations imposed on the provider under the Act or any contractual arrangement...*

## Suitability

The title of paragraph 8 of the General Code of Conduct is *suitability*. As this term is not defined in the Act or the Code, we must use its normal meaning. *Suitable* is defined as *right or*

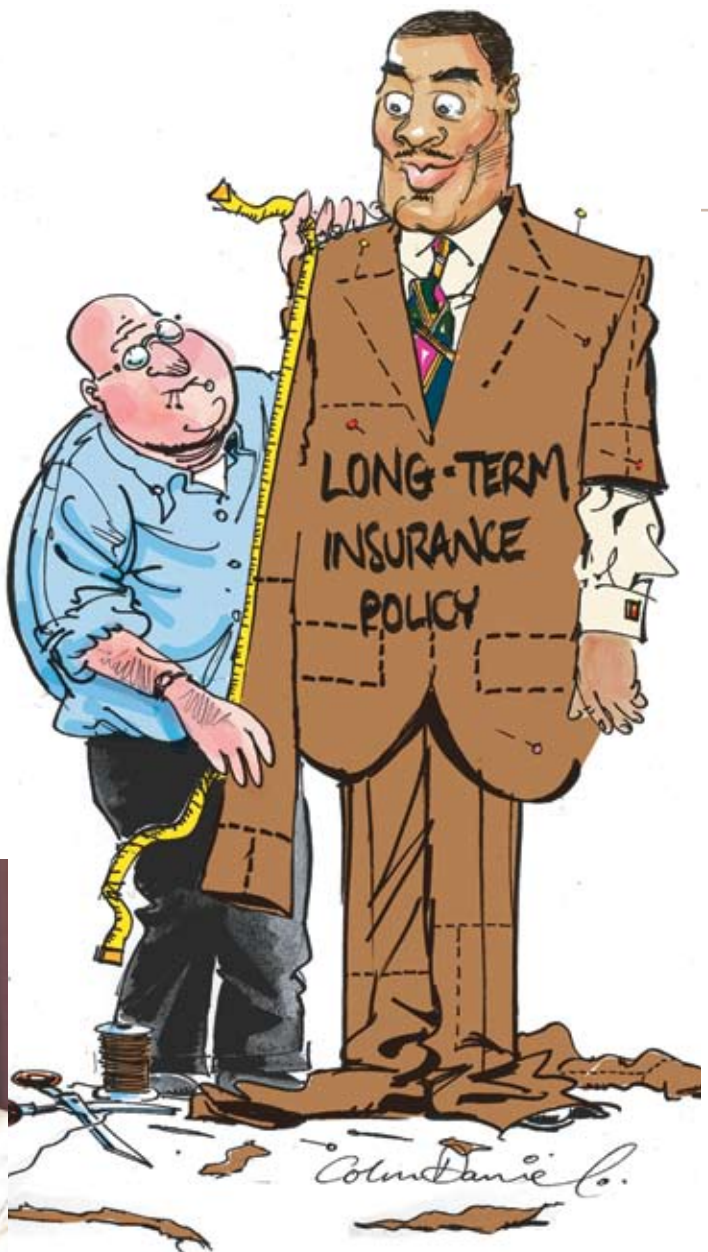


*appropriate for a particular purpose or occasion.*<sup>1</sup> In terms of the language of the Financial Advisory and Intermediary Services Act (FAIS Act), 2002, it could be translated as *right or appropriate for the client's purpose, risk profile and financial needs.*

## Suitability test

How would one determine whether a long-term insurance product will pass the suitability test? This is an important question as it is the question that the FAIS Ombud will have to answer when a complaint serves before him.

This article aims to put financial services providers in a position to answer that question long before a client complains. Being pro-active is the first of Stephen R. Covey's *Seven Habits of*



*Highly Effective People.* Providers will do well to consider the suitability test as part of their risk management plan. There are four key considerations when it comes to the suitability test. They are:

### 1. The client's needs and objectives

Financial needs have not been defined in the FAIS Act and therefore we use the word's normal meaning. *Financial* means "connected with money and finance"<sup>2</sup> and *need* means "to require something because (it) is essential or very important, not just because you would like to have (it)"<sup>3</sup>.<sup>4</sup>

Objective is defined as *something that you are trying to achieve*.<sup>5</sup> It would appear from paragraphs 8(1)(a) and 8(1)(c) of the General Code of Conduct that client's financial needs and objectives are closely related.

The only way providers can act in the interest of clients as required in the General Code of Conduct is to ensure that they understand the client's needs and objectives.<sup>6</sup> This requirement contributes to the professional relationship between provider and client.

Offering client-centered advice is vital if providers want to establish a trusted client relationship. Therefore, providers should always start with trust in mind. When establishing trust, compliance will follow automatically.

**Example:**

Malcolm X needs the following insurance benefits:

- R 2m life cover;
- R 1m capital disability;
- R 30 000 per month income in the event of permanent disability; and
- R 500 000 trauma cover in the event of cancer or suffering a heart attack.

## 2. Risk profile

*Risk* means the *possibility of something bad happening or a situation that could be dangerous*. To risk something is *to do something even though the result could be unpleasant*.<sup>7</sup> *Profile* is a description of something that gives useful or important information.<sup>8</sup> A person's profile may also be defined as a *character sketch*.

**Important notice:**

Risk profiling does not only apply to investments. It also applies to long-term insurance policies.<sup>9</sup> A client who applies for disability benefits has a different risk profile compared to a client who may need disability benefits but does not include it in his/her insurance application.

The latter is willing to accept a higher degree of potential loss in the event of disability. A client, who cannot afford not to be covered in such cases, may get desperate should he/she become disabled.

The risk for the advisor is that the client may be tempted to blame the advisor for not including disability in the application. Therefore it is necessary

to establish a client's risk profile before submitting the policy application to the life office/product supplier.

**Example:**

Malcolm X decides *not* to include the disability income benefit and lump sum trauma benefit, despite the risk of permanent disability and trauma. The client's decision affects his risk profile and the provider needs to record the decision and get the client to verify it in writing.<sup>10</sup>

## 3. Key features and benefits of proposed product

To establish whether the financial product would be appropriate for the client's purpose, risk profile and financial needs, the most logical test would be to compare the client's needs, objectives and risk profile with the key features and benefits of the proposed financial product.

**Example:**

As stated, Malcolm X required the following insurance benefits:

- R 2m life cover;
- R 1m capital disability;
- R 30 000 per month income in the event of permanent disability; and
- R 500 000 trauma cover in the event of cancer or suffering a heart attack.

However, he decided to accept the risk in the event of disability (income) and trauma. His final request only included:

- R 2m life cover; and
- R 1m capital disability.

The financial proposal would meet the suitability requirement if the provider proposed a policy quotation of:

- R 2m life cover; and
- R 1m capital disability.

The provider in this case clearly considered the client's needs, objectives and risk profile. However, the client's decision and agreement must be recorded and signed by the client. This would be vital because the advisor would be at great risk if the client later alleges that income and/or trauma was also a requirement.

## 4. Disclosure of material terms, conditions and exclusions

Paragraph 8(1)(c) of the General Code of Conduct has a provision, namely: *identify the financial product or products that will be appropriate to the client's risk profile and financial needs, subject to the limitations imposed on the provider under the Act or any contractual arrangement...*

Product providers offer life and disability cover subject to certain terms, conditions and exclusions. It is therefore important to disclose these terms, conditions, exclusions and other disclosures<sup>11</sup> as it would determine whether the product will pass the suitability test. Fees and/or commission could be considered part of the policy's terms.

### Value of a signed quotation

Product suppliers offering long-term insurance products are generally fairly good with their disclosures of key features, benefits, terms, conditions and exclusions in their quotations.

Unfortunately some financial services providers still do not get the client to sign every page of the quotation as evidence of his/her acceptance of the financial product proposal. If the client signs the quotation on every page, it offers evidence that the necessary features and terms, conditions and exclusions have been disclosed. More importantly it offers evidence that the client accepted the proposal, **subject to the limitations imposed on the provider under the Act or any contractual arrangement...**

Three of the five vital elements necessary to pass the suitability test are contained in the quotation, namely:

- Key features and benefits of the long-term insurance policy
- Terms, conditions and exclusions
- The cost

The other two elements (needs/

**Continued on p 6**

# Regulation must strike the right balance

**The challenge of supervision and regulation is striking the right balance between restrictive regulation and laissez-faire deregulation. In striving to strike this balance, the FSB is helped by its mandate, which tasks it with protecting consumers and engendering a sound financial environment for the entities we regulate and supervise. This is the message of Abel Sithole, chairperson of the FSB, in his chairperson's review in the FSB's latest annual report.**

"The year under review has again been a challenging one for the FSB. The challenges of regulation and supervision have been set against the backdrop of the global financial crisis and its effects since the crisis first manifested in early 2007. There has been disruption in international financial markets, high international and domestic inflation, the slowing of domestic growth and huge job losses locally and internationally. South Africa is now in a recession, which will adversely affect consumers and the entities that the FSB regulates and



**Abel Sithole, chairperson of the FSB Board**

supervises.

"Many analysts and commentators ascribe the crisis to the highly deregulated and leveraged US financial system which accumulated and accentuated systemic risks. This has resulted in calls to review financial market supervision and regulation to bolster and build a more

resilient financial system locally and internationally. There is therefore the risk of overreaction that may lead to overly tightening regulation to the extent of stifling legitimate financial development and innovation that oils the functioning of the financial system," Sithole said.

Globally, growth is expected to fall to its lowest level since World War II. The IMF forecasts a total budget deficit of seven per cent of GDP for advanced economies for the 2009 financial year. This will affect the livelihoods of almost everyone in an increasingly inter-connected world.

He pointed out that although South Africa will not be immune from the effects of this crisis, which have affected the real economy, the country's regulatory system has stood up well to global market turbulence. "We were largely buffeted for a number of reasons: Our stringent prudential regulations, the prudential investment guidelines that limit the extent of assets that can be invested offshore, foreign exchange controls and the National Credit Act, 2005 among others. The recent World Bank Financial Stability assessment gave South Africa's regulatory framework the thumbs up," Sithole said.

## Suitability test continued from p 5

objectives and risk profile) should be covered in the advice agreement<sup>12</sup> between the parties. The signed quotation is an extension of the advice agreement.

It is important to understand that while the client may need disability and trauma benefits, the client's risk profile and/or ability to pay the premium on the full benefits, may have a limiting effect on the policy benefits.

If the client cannot afford the premium on a policy that is suitable for his/her needs, that will be a

legitimate reason for applying for a policy which offers less cover than necessary. Based on affordability, the policy cover may be reduced and will still meet the requirement of suitability. The key however is recording of the circumstances and making sure that the client signs the necessary documentation.

### References

- <sup>1</sup>Oxford Advanced Learner's Dictionary, p. 1480
- <sup>2</sup>Oxford Advanced Learner's Dictionary, p. 551
- <sup>3</sup>My insert
- <sup>4</sup>Oxford Advanced Learner's Dictionary,

p. 979

<sup>5</sup>See Oxford Advanced Learner's Dictionary: p.1005

<sup>6</sup>See paragraph 2, 8(1)(a) and (c) of the General Code of Conduct

<sup>7</sup>See Oxford Advanced Learner's Dictionary: p.1264

<sup>8</sup>See Oxford Advanced Learner's Dictionary: p. 1160

<sup>9</sup>See paragraph 8(1)(c) of the General Code of Conduct

<sup>10</sup>See par 3(1)(d), 8(1)(c) and 9 of the General Code of Conduct

<sup>11</sup>See par 7 of the General Code of Conduct

<sup>12</sup>See section 20(3)(a) of the Act and paragraphs 3(1)(d) and 9 of the General Code of Conduct

The FSB's 2009 annual report was tabled in Parliament in September.



**Although the FSB was stretched in terms of resources to discharge its regulatory and supervisory role against the background of extremely challenging times for the financial markets of the world, the Board rose to the occasion and sent a clear message to industries that there is a strong and caring regulator. So said Dube Tshidi, executive officer of the FSB, in the Board's 2009 annual report.**

"It has been another tough but exciting and rewarding year for the FSB and we have fine-tuned our strategic plan based on market conditions," Tshidi said.

"As regulators, we must remain vigilant and will continuously evolve and improve our watchdog role. Our focus for the review period was on managing the financial crisis and assisting the business players in our markets to cope with the challenges that have become part of our financial lives. This called for honest self-introspection and how we go about performing our regulatory role. We have learnt valuable lessons from this crisis and as such, our approach to regulation has changed going forward. Our work for the past months was characterised by the following efforts:

- Managing the effect of the financial

# Tough but exciting year for FSB

crisis as experienced by the entities that we regulate.

- Intensively supervising the entities we regulate through on-site visits. This has resulted in our on-site teams being stretched.
- Maintaining focus on our risk-based supervision.
- Doubling the efforts of the Consumer Education Department to ensure that consumers receive assistance to stay in control of their finances, particularly investments.
- Continuing to regulate our markets to ensure efficient, fair and abuse-free trading and managing the interrelationship between the exchanges to maintain the confidence of investors.
- Making the necessary improvements to our organisation's effectiveness by improving our infrastructure, employing people with good skills and placing them in the right jobs.

"We have also introduced stress-testing which will assist in detecting and managing potential systemic risks. The FSB is also embarking on a major project to introduce the "Treating Clients Fairly" concept throughout our business practices and regulated industries.

"Over the past few years the FSB's scope has increased tremendously and we had to concomitantly increase our staff complement. However, we were not able to fill all our posts for two reasons: firstly a lack of space, and secondly, being aware of the difficulties the levy payers are experiencing. In 1999 our staff complement was a mere 132. This year it is at 411 (including contractors).

"On the legislative front, the General Financial Laws Amendment Act (GFLA) passed by Parliament in 2008, closed loopholes in existing legislation while at the same time giving the Registrar



**Dube Tshidi, executive officer of the FSB**

additional enforcement capabilities.

"Regarding our social responsibility, our consumer education plan has seen us promoting programmes and initiatives by financial institutions and bodies representing the financial services industry to inform and educate users and potential users of financial products and services.

"We will continue to interact with regulatory bodies in other jurisdictions to ensure that our standards are world class. The FSB participates in international and regional regulators' forums and we are pleased to have won the bid to host the annual conference of the International Organisation of Securities Commissions (IOSCO) in 2011. This is a vote of confidence in South Africa in general and the FSB in particular," Tshidi said.



# The slow but tenacious wheels of justice

By Gerhard van Deventer,  
executive director, Directorate of  
Market Abuse, FSB

**On 20 August 2009, Jacobus Bezuidenhout was sentenced in the Regional Court in Bloemfontein for contravening the Close Corporations Act, 1984, five counts of theft of approximately R350 000 and one count of fraud involving about R100 000.**

It must have been cold comfort for him that the magistrate gave him the benefit of the doubt on another five counts of fraud and two counts of contravening the now repealed Stock Exchanges Control Act, 1985.

After a quick calculation of the

sentences running concurrently, it became clear that Bezuidenhout would stay as a guest of the state for the next three years and nine months.

Bezuidenhout used his charm and the trusting personalities of his Bloemfontein clients to convince them to hand over their hard-earned money for “investing”. He marketed himself as an able investment manager but had at best a very modest knowledge of the topic. The only other two employees in his business were students.

But it was not necessary for him to know much about investments, because he used most of his clients’ funds to pay personal expenses, such as telephone accounts, school fees and medical bills.

In cases where clients’ funds *were* indeed invested in securities, his lack of skill was obvious. He ignored basic risk management and made investment decisions on “tip-offs”. Most of these funds were lost. But it was not *his* funds and certainly not *his* losses.

Bezuidenhout did not apply for FSB

approval. He explained that he had the good intentions to do so, but it slipped his mind. He also did not keep proper records of his clients’ funds and assets, and his brother who lived in the Cape wrote his books and records up “periodically”. Needless to say, these books and records were not available when the FSB investigated his activities. The Magistrate’s clear-cut judgment was in stark contrast with Bezuidenhout’s original reassurances to the FSB that he was not investing clients’ funds.

He explained that he was merely doing them a favour by keeping an eye on some of their investments. That is of course except for the senior citizen whose funds he invested in his personal trust “by accident”. He ignored the FSB’s instruction to stop his investment management activities until he is licensed as a financial services provider.

But Rome was not built in a day. Bezuidenhout committed the offences between 1997 and 2001. At that stage

the FSB received a few complaints and ordered an investigation. The investigation was completed in 1998 and the matter was referred to the SAPD's Commercial Crimes Unit in Bloemfontein.

The attorney-general of the Free State became involved, but eventually it was decided to prosecute the case in the Bloemfontein Regional Court. After Bezuidenhout was arrested and granted bail, the matter was postponed for to

January 2000 for trial.

At this stage Bezuidenhout decided to exercise his many rights as an accused, and brought some applications that were destined for the Constitutional Court. After a few postponements, Bezuidenhout had to eventually face his day in court in 2003. He must have decided that standing trial was probably not his best option, because he did not turn up for his hearing. Consequently, his name was circulated by the South

African Police Services (SAPS) as a "person on the run".

During 2004, the SAPS found Bezuidenhout and brought him to court, but he was granted bail. His case was eventually heard in 2009, 13 years after his first offence!

At last justice was done and the weary prosecutor could close his file. Bezuidenhout has still not applied for approval to be an investment manager.

## CRG faces probe by FSB and the police

### Central Rand Gold (CRG), the junior mining house, is being investigated by the FSB and the police.

The FSB's executive director of market abuse, Gerhard van Deventer, confirmed that the regulator would investigate allegations that CRG had issued false information to its investors.

"We have received a complaint and we are investigating allegations that the company has historically been giving false information. We are still investigating and we don't know what the outcomes will be yet," he said.

The FSB inquiry comes as papers before the Gauteng South High Court have revealed that the serious economic offences unit of the SAPS is also investigating the JSE-listed mining firm over allegations of issuing false information and withholding information from the company's shareholders.

In the papers brought by Puno Gold Investment (PGI), CRG's empowerment partner with a 26 percent shareholding, PGI is seeking an interdict to stop CRG from mining until it consults with its partners.

PGI has filed a complaint of non-

disclosure of material information to investors and falsification of information. The court papers also allege that CRG management was engaging in activities that bordered on fraud involving millions of rands, reckless and unauthorised expenditure and inflated invoicing.

PGI had approached the JSE in November last year with the same allegations.

In June the FSB informed CRG that it was carrying out the investigation.

"This serves to inform you that we will be carrying out an investigation of market abuse in terms of section 82 of the Securities Services," the notice read.

#### Parties notified

The FSB notified the parties of an extension of the investigation in September.

The two companies are still facing an arbitration related to a dispute sparked by CRG's financial demands last year. Then CRG wanted PGI to contribute R72 million as part of the company's budgeted expenditure and the mining company took up a call option over PGI's stake in CRG.

In May the South Gauteng High Court ruled against CRG's actions until the matter was resolved by arbitration or court proceedings. PGI also filed an



Gerhard van Deventer

interdict to stop CRG from mining in certain tenement areas.

PGI argued in court papers that, according to their shareholder agreement, the companies were to enter into negotiations with a view to reaching consensus on the basis upon which a mine could be developed once a bankable feasibility study had been done. But PGI alleged that the company had been mining since last year without honouring this agreement. CRG could not be reached for comment.

**Source: Business Report, 14 September 2009**

# Save us from

By Abel Sithole, chairperson of the FSB Board

The cost of dying should be a major policy issue in South Africa. According to StatsSA there were over 600 000 registered deaths in 2006, a number that has doubled from ten years earlier. This means that one in forty South Africans is directly, and about one in four indirectly, affected by death every year.



**The estimated direct contribution to funeral expenses by those who do so from their own pockets is around R3 000 which is almost half the annual State Old Age Pension. So guess where a big chunk of granny's pension is going!**

Death is a certainty and part of our lives. We should prepare for it. For those left behind, death entails a double loss: the loss of a loved one, as well as the unwelcome but tolerated expense. Without planning, this expense places a great burden on survivors.

Industries have mushroomed around the committal of mortal remains with varying degrees of formalisation, organisation and legitimacy; from the providers of funeral insurance to undertakers, from the providers of coffins to the printers of obituaries and funeral programmes.

These industries provide a very useful service. However, they also add to the cost of dying which in South Africa is borne disproportionately by middle income and poor black families. This does not mean that other socio-economic groups do not incur death-related expenses, but they tend to be

able to contain them. Most discussions about the burden of the cost of dying is focused on formalisation and legitimisation of industry players.

Research from Finmark Trust released in May 2005, showed that South Africa's poor are frequently burdened with having to pay for unexpected events, in particular funerals and traditional feasts. Subsequent studies have confirmed this reality. The "most frequent financial event" to which families had to contribute was the funeral of a member of the extended family, work colleague or friend. The burden of the cost of death presents an

# the cost of death

extensive demand on earnings compared to other costs such as food and clothing. Death robs people of their loved ones and hard earned cash. It puts people in debt and reduces ordinary people's propensity to save. Hence the argument that the cost of dying should be a major policy issue in South Africa, especially in the light of growing calls for South Africans to save and reduce debt. The amounts of money currently going to burial societies, funeral policies and paid directly to meet funeral expenses could be channeled elsewhere, including savings.

Unfortunately the burden of the cost of dying is often couched as an indication that the majority of South Africans are underinsured and as an opportunity for the insurance industry to meet a genuine need. This could not be further from the truth. The burden of the cost of dying arises from prolonged and lavish funeral rituals. To alleviate it does not require being insured but readjusting funeral rites.

## **Making expenses affordable**

Death, especially funerals need not be expensive. A number of easy changes such as leaving clear instructions about how to be treated after death, minimising the time from death to committal of the body and removing frivolous trappings and paraphernalia that surround the funeral rites can reduce cost drastically.

## **Planning**

A big contributor to the cost of death is lack of planning. Due to lack of clear guidance from the deceased on how their remains should be interned, the living are left with having to do what they believe is best, as well as focusing on how they "look". Unless the deceased has made his/her preference clear in advance, the living will seek to appease

the dead through a lavish and expensive funeral.

## **Expediting the committal of remains**

The traditional funeral rites probably last on average between one and two weeks. During this time costs are incurred to keep the body at the mortuary and to feed those who come to offer condolences. The body often gets transported great distances to be buried "at home" at great expense. Then there is the feast following the burial. By honouring and sending off the dead with dignity, everything is done to show off the material and financial capability of the living. This leaves behind debt and suffering.

There is no logical reason why it takes so long to bury the dead among those who can least afford it. The burial should take place in the shortest time possible after death.

This could be within 24 to 48 hours of death as practiced in certain traditions, cultures, religions and countries. Instead of the current prolonged funeral rites, a funeral that takes place within a day or two of death would cut costs drastically.

## **Saving costs**

### *Coffins*

Coffins are wooden boxes that are cheaply made and then embellished and sold at exorbitant mark-ups. There is no reason why cheap coffins made of cheaper alternatives such as cardboard cannot be used.

### *Burial plots and gravesites*

The cost of burial plots can be eliminated by substituting burials with cremation. Cremation is cheap and saves land, currently set aside for cemeteries. In the past decade another new expense has been introduced: Walling-in of graves and covering them in concrete

to prevent theft of coffins. With the use of inexpensive coffins this becomes unnecessary.

### *Feeding the funeral cortège*

Funeral services often take unnecessarily long as a result of those paying their respects or offering eulogies. This results in people needing to be fed after the service. Some communities practise the option of "bring and share" to alleviate expenses. "Bring and share" is also great for solidarity.

### *Dispensing with the theatre*

Funerals are getting more theatrical. There are now ushers and hosts in fancy dress that accompany the hired equipment, not to mention the flowers and limousines. The ancestral and cultural origins of imported flowers and limousines in the black South African context still need some explanation.

### *The policy response*

It is unlikely that a democratic country like South Africa will prescribe how its citizens should commit the remains of their loved ones. It is also unlikely that government will prescribe a standard inexpensive coffin or funeral, although this may be no more intrusive than the smoking ban in public places or the use of plastic shopping bags.

There are also administered prices for electricity, petrol, etc. Government, unions, religious institutions, NGOs, etc can, however, consider education campaigns to sensitise citizens to the cost of funerals and strategies to alleviate costs.

The financial relief this will provide to middle income and poor South Africans burdened with the yoke of funeral expenses will be immeasurable as will be the freedom from the related bondage of socio-psychological pressure to "stage" a funeral to remember.



# Be aware of your funeral benefits



By Judge Brian Galgut, Ombudsman for Long-term Insurance

**It is of concern that beneficiaries, whether they are members of funeral schemes or policyholders are sometimes unaware of what exactly they are or are not covered for. It is important that schemes, their members, and policyholders check their benefits to avoid disappointment.**

In the latest newsletter of the Office of the Ombudsman for Long-term Insurance (Issue 11, June 2009), attention was drawn to two cases dealing with funeral schemes. Both involved group schemes that were the policyholders, where the question arose whether the scheme members had been aware of certain relevant policy terms that affected their claims.

In the first case a funeral policy

contained a clause terminating a group scheme member and his or her spouse's cover on the person's 65th birthday. We received a complaint from a spouse whose husband had died at the age of 67. Her claim had been rejected by the insurer because the policy had contained such a clause. We could not assist with the complainant because the insurer's contention fell fully within the relevant term of the policy.

## **Concerned**

We nevertheless remained concerned about the effect that such a term can have on lives assured, because to terminate cover at age 65 is to do so at a time when it is most needed, and when it would be difficult for the lives assured to obtain cover elsewhere.

In the second case the group funeral scheme had been arranged through a labour union. The policy provided that, when retiring and thereby ceasing to be a member, the member could apply within six months of retirement for a paid-

up policy. Such an ex-member would thereby retain cover, without having to pay any further premiums.

The assured died some years after retirement and the death claim was declined because he had failed to apply for a paid-up benefit either within the six month period or at all.

## **Unaware**

The complainant, the deceased's son, contended that the deceased had been unaware of the option concerned. He stated that the deceased had not been directly furnished with the terms and conditions of the policy, that he had been illiterate and that he could not have been expected to know the policy rules unless specifically alerted thereto by the insurer.

In response the insurer stated that it had informed members through "road shows" and had asked labour union shop stewards to advise members of the group scheme about the policy provisions and

*Continued on p 13*

# FAIS conferences provide valuable communication opportunity

**“The annual conferences of the FSB’s FAIS Department provide the Board with an excellent opportunity to communicate with financial services providers (FSPs) in person. Although we use various other methods to communicate with the industry such as our regular newsletter, this personal contact with FSPs is of great value,” says Wendy Hattingh, head of the FAIS Supervision Department of the FSB.**

The conferences this year took place in Pretoria and Cape Town and were fully booked only days after registrations opened. “The interest in Cape Town was such that we had to organise a second conference to accommodate all. In total 1 100 FSPs attended this year,” says Hattingh.

The FSB first presented the FAIS conferences in 2008 and according to Hattingh, the Board aims to make this an annual event.

“The conferences give us the opportunity to engage in robust debate with the industry. Not only can we explain FAIS procedures and regulations but the feedback from FSPs on what works for them and the practical hiccups they encounter, is of great value to us.



FSPs at the Pretoria conference

FSPs for instance pointed out areas of concern that need stronger regulation by the FSB.”

The industry was well represented at the workshops. According to Hattingh key individuals, representatives, training managers, HR managers and compliance officers from various companies and institutions were among the delegates. “Some were even from other provinces

such as the Eastern Cape and Mpumalanga. Cooperation by various departments of the FSB as well as other regulatory bodies such as ombud offices and organisations such as the Association for Savings and Investment (ASISA) and the Financial Intelligence Centre (FIC) made the conference a huge success,” says Hattingh.

## Funeral benefits continued from p 12

requirements.

The relevant information may have come to the knowledge of the deceased, but there was no certainty about this. Any general departure from the policy terms would of course affect the fundamental actuarial assumptions behind the policies, the paid-up reserves, the solvency of the group scheme, and the inevitable consequence that there would be an increase in premiums.

We came to an understanding with

the insurer that the claim in question would be paid on an ex gratia basis.

It is of concern that beneficiaries, whether they be members of schemes as such or the policyholders themselves, are sometimes unaware of what exactly they are or are not covered for, a problem that is not of course limited to group schemes or to funeral cover.

The above two cases illustrate just how important it is that both schemes themselves, their members, and policyholders generally should always check their benefits to avoid disappointment.

# Is South Africa's financial sector robust? Findings of the latest FSAP

By Elias Masilela, head of Corporate Affairs and Retirement Reform, Sanlam Group

**In hindsight, one cannot help but conclude that South Africa's Financial Sector Assessment Programme (FSAP) undertaken by a joint team of the IMF and World Bank, could not have been better timed.**

This assessment was completed in August 2008 and published under the title "Financial System Stability Assessment." This was exactly a year after the emergence of the sub-prime crisis that has resulted in the now insufferable economic meltdown.

## **What is a FSAP?**

"A Financial Sector Assessment Programme is a process to assess or evaluate the stability of the financial system in a country as a whole and not that of individual institutions. They have been developed to help countries identify and remedy weaknesses in their financial sector structure, thereby enhancing their resilience to macro-economic shocks and cross-border contagion. FSAP assessments do not cover risks that are specific to individual institutions such as asset quality, operational or legal risk or fraud." South Africa FSAP 2008 (p.1)

Countries elect to have this

assessment undertaken and also whether or not to share the details of the report with the rest of the world. South Africa was among the first, if not the first developing country to have subjected itself to this exercise. South Africa also took the up-front decision to make the report public, as part of Government's comprehensive programme of deepening transparency. In August 2008, the Joint FSAP team concluded that South Africa's financial sector is sound and seems to be weathering the storm: "South Africa's sophisticated financial system is fundamentally sound and has so far weathered the global financial market turmoil without major pressures. Banks and insurance companies have enjoyed good profitability, capitalisation levels and reserves."

"However, the system faces heightened macro-financial risks and financial institutions are bracing for a less benign environment. Stress tests suggest that capital and reserve cushions at banks and insurance companies are sufficient to absorb large shocks." (p.1) One of the key exercises undertaken by an FSAP team visiting any country, is to stress test the financial system. This is done through a modelling exercise, which is sometimes criticised for being too idealistic. With the advent of the sub-prime crisis, which caused current economic weakness across the globe, there is no better stress test to ask



for. Should the South African financial system show resilience under these circumstances, no one will remain in doubt about its robustness as well as regulatory regime. However, the jury is still out. An assessment towards the end of 2010 would be more than appropriate.

## **Why is it of interest to the insurance and pension sector?**

As rightly observed and stated in the FSAP report, "Insurance companies are major players in the South African financial sector. A key reason for the scale and significance of the life insurance sector is its large share of the retirement savings market." (p. 26.) Given the strategic importance of this sub-sector it will always be the pace setter in the economy.

This is the second assessment to have been undertaken in South Africa. The first was done in 2001. The key difference between the two is that the 2008 report is the first to have delved into the insurance and pension sub-sector, having noted



the importance of these areas to the economy. This was also triggered by the huge policy debate unfolding in the country on social security and retirement reform. This process is affected by what happens in the macro and micro economy.

According to the IMF, "Insurance penetration (in SA) – premiums in relation to GDP – is among the highest globally at 16%." (p. 26.) It is common knowledge that life company assets are significant in South Africa, estimated at about 80% of annual GDP at the end of 2007. The strong correlation between the economy and the financial sector is well established.

The recent economic upswing has benefited the financial sector, resulting

in rising surpluses in excess of the relevant regulatory minima. However, with the economic fortunes having turned, the outlook does not look as rosy, with high interest rates, slowing economic performance and subsequent reduction in employment. These factors combined are forcing an increase in lapses and surrenders. Undoubtedly that all insurers are singing a different tune regarding the generation of new business. This may well be the case until sometime in 2010.

The interplay between the state of the economy and the financial sector will remain an important relationship to be watched over the next 18 months. Ironically, the FSAP report also raises the social security and retirement

reform process as one of the key developments to be watched, "The Government's planned retirement and social security reforms, depending on their final shape, could lead to a drain of both retirement savings and protection business in favour of mandatory contributions to state insurance funds." (p. 27.) This is not only in relation to developments in the financial sector - these are concerns echoed by the private sector. Clearly, there is a good case to watch these developments closely as they unfold.

It is also interesting to note the unequivocal support from the FSAP

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## Part 1



Bringing financial literacy to the people. The FSB's Consumer Education Team are from left: Olivia Davids (head), Peter Bosch, Laura Masemola, Ginger Bester, Linda Makhubo, Lyndwill Clarke, Elliot Modisa, Panama Mphanama and Lynette van der Merwe

# Consumer education finding its feet in South Africa

**Consumer education is finding its feet in South Africa. In this article, the first of two, Olivia Davids, head of the FSB's Consumer Education Department, tells about the success of the past years.**

"Among the successes of the FSB's Consumer Education Department (CED) since it started operating in 2004 is the access to schools established through the Department of Education. We have also created many networks in various spheres of the community that enables us to promote financial literacy among consumers. Consumer education, as with education in general, is however long-term and it remains difficult to measure success in the short term," says Davids. "It is clear that South Africa is playing

a significant role in educating consumers on financial issues. Many countries use our experience as a model to develop consumer education in their countries. The FSB receives numerous requests for information and also for opportunities to spend time with the Consumer Education Department of the FSB," Davids says.

The FSB this year organised a consumer education familiarisation programme for 20 representatives of the Committee of Insurance, Securities and Non-banking Authorities (CISNA). Among this group were representatives from West and East Africa as well. The aim of the five-day programme was to assist other regulators in developing consumer financial education programmes and strategies, using South African models as examples, and adapting these to their own needs and situations.

Among the many projects of the CED, teacher development remains a priority.

"We have developed mathematical literacy resources called *Managing your money* for Grades 10, 11 and 12. They are in lesson plan format with posters and CDs. The resources are mediated to teachers and subject advisors through workshops which started in May this year. Four thousand teachers and subject advisors have already been trained in 59 workshops. This project is conducted in partnership with the South African Insurance Association and the Department of Education," says Davids. Other CED projects include:

### **FSB consumer education booklets**

"The FSB's educational booklets on budgeting, saving, banking and insurance have now been revised and translated into Afrikaans, Sepedi, Sesotho, Xhosa and Zulu. The booklets are aimed at LSM 1 – 10 and are used at

various workshops. They form the basis of all our educational initiatives.

### Digitising consumer education booklets

The booklets have also been adapted in line with the National Curriculum Statements (NCS) for Mathematic Literacy and EMS and introduced to schools as part of the Money in Action project. This resource is CD rom-based and is accompanied by four booklets for schools without an IT infrastructure.

### Community-based workshops

After a pilot of 60 workshops in KwaZulu-Natal and the North West Province in 2007, the CED decided to extend these to all provinces.

These financial literacy workshops are based on the FSB booklet 1 which deals with budgeting and saving. It targets consumers in LSM 1-5. The workshops started in June this year and are proving

to be very popular among consumers.

The CED has already hosted 85 such workshops.

"A phone-in support system is provided by the service provider for a period of three months following attendance at a workshop," Davids says.

### Financial guide for youth

The CED has compiled a financial guide for young people that addresses various financial issues such as opening a bank account, debt management, income tax and savings.

The guide is aimed at young people between 18 and 22 and 108 workshops have been held with 3 010 participants across South Africa. Davids says: "It was encouraging to see young people being inspired to become financially independent."

*(Continued in our next issue.)*

**Right: Among the many projects of the CED, teacher development remains a priority. Four thousand teachers and subject advisors have already been trained in 59 workshops.**

**Below: Career exhibitions are also on the CED's menu. This group of students learns more about financial issues at an exhibition at Bisho in the Eastern Cape.**



## FSAP findings continued from p 15

team for:

- A shift from lump-sums to income
- More stringent draw-down rules to deal with longevity risk
- Preservation until retirement
- Education and training, in particular of trustees to understand their fiduciary duties, to the extent of enforcing fit and proper requirements
- Improvement in compliance and consumer protection
- Consolidation of the industry for regulatory purposes
- Conversion of circular PF130 on good governance of retirement funds into an enforceable regulation.

### Conclusion

It can only be in the best interest of South Africa to ensure stability, robustness of the financial system, and deepening of trusted regulation and supervision. There is no doubt that we are reaping the benefits of a sound regulatory environment, developed over decades. This has to be protected and preserved, as it will always be the insurance in difficult economic times such as these. If we believe that the financial sector is the engine of the economy, it will drive the growth and wealth creation that we desire as a society. Any attempt to stifle the creative role of the financial sector, would be thrashing the fortunes of South Africa and undermining an investment of many lifetimes.

**Source: Excerpt from Insight, March 2009**



Photo: AE Hejdenrych

## Economic outlook

# South African economy set to recover in 2010

By Flip Meyer\*

**The South African economy is set to recover in 2010. The year 2009 will post negative economic growth in a time when the world has suffered a severe recession.**

The 33 economists, who participate in the Economist of the Year Competition of Finmedia24, predict a negative growth rate of -1,36% for this year and a modest positive of 2,43% next year. Clearly South Africa has not escaped the cold winds of the international crisis. The road to recovery will be a long one.

In January 2009 these economists' consensus prediction was a positive +1,14% for 2009. Ten months ago the recession was clearly underestimated. The year 2009 has been a nightmare for any economist. Predicting the future must be one of the most difficult jobs in the world. The views of some then that South Africa would not be affected by the melt down in the USA and Europe were wrong and naive.

The stock markets of the world have been recovering in August and in September discounting a recovery. Stock markets anticipate future events.

Some critics say the stock markets have overreacted and discounting improvements in the international economies far too soon.

The South African stock market followed the international optimistic trend. When share prices on the stock exchange in New York recovered, the same happened in South Africa the next day.

The Dow Jones index, the barometer of the US stock market, has risen to the same levels last year before the huge turmoil and shrinking experienced early in 2009.

The stock markets do not reflect current dire economic situations. But there is a good reason why.

Chris Freund, manager of Investec Asset Management, says there is nothing irrational about the way the South African equity market has behaved. From March to September the local market improved by about 40%.

In almost every past recession the stock markets started improving rapidly once there was a reasonable certainty that the rate of economic decline is starting to slow. "Markets start to price in improving prospects of the future and historically this part of the equity cycle has offered the highest returns," says Freund.

The current crisis became visible with

the collapse of Lehman Brothers on 15 September 2008. This prompted a huge response from governments and central banks to contain the effect of the financial crisis on economies. Stock markets reacted and the crisis was reflected by the sharp decline in share prices worldwide.

The fear factor moved in and investors panicked. Some sold their stocks. The rest is history.

Fear, like greed, leads to irrational behaviour. In times of bull markets the greed factor steps in and this leads to investors buying shares at high levels just before markets fall. Either way, people lose money if the human factor dominates their investment decisions.

Credit and loans from banks dried up and businesses had to close down.

Not many people would have expected a recovery but it happened and those who bought close to the rising trend in share prices thereafter have made money.

One should not be too critical because it is almost impossible to predict the short-term future.

Jac Laubscher, group economist of Sanlam, says highly divergent views prevailing are a severe reminder that in the current economic climate forecasts are even more uncertain than usual. He says South Africa must refrain from bold statements and rather acknowledge that the abnormal nature of this recession makes an abnormal outcome highly likely.

"We find ourselves at a point in time where the contraction in growth has probably run its course. Some countries, like Germany, France, Brazil, China and Japan are already in the snap-back phase, while others (including South Africa) are still lagging," says Laubscher.

The value of the Economist of the Year Competition eliminates a lot of risks described by Laubscher. The more economists participate in the competition, the more their consensus prediction may become reality in future. These economists also have the opportunity to revise their predictions

every month. Predictions made in January of each year would probably look quite different than the last predictions made in December. Unexpected events are taken into account.

Some of the trends economists predicted in 2008 have become reality. They are:

- A decline in the inflation rate;
- Several interest rate cuts, although the end of this trend is in sight;
- Slower economic growth, although most economists did not predict that 2009 would end up in the negative zone;
- Declining exports due to the poor economic conditions prevailing in countries, normally the important trading partners of South Africa.

Over the short term it is impossible to predict the value of the rand because so many external factors play a role. In September the value of the rand strengthened against the US dollar. Movements in the value of the US dollar have a direct effect on the value of the South African currency. However there are signs that foreign investors favour emerging markets such as South Africa.

Inflows of investment keep the value of the rand strong.

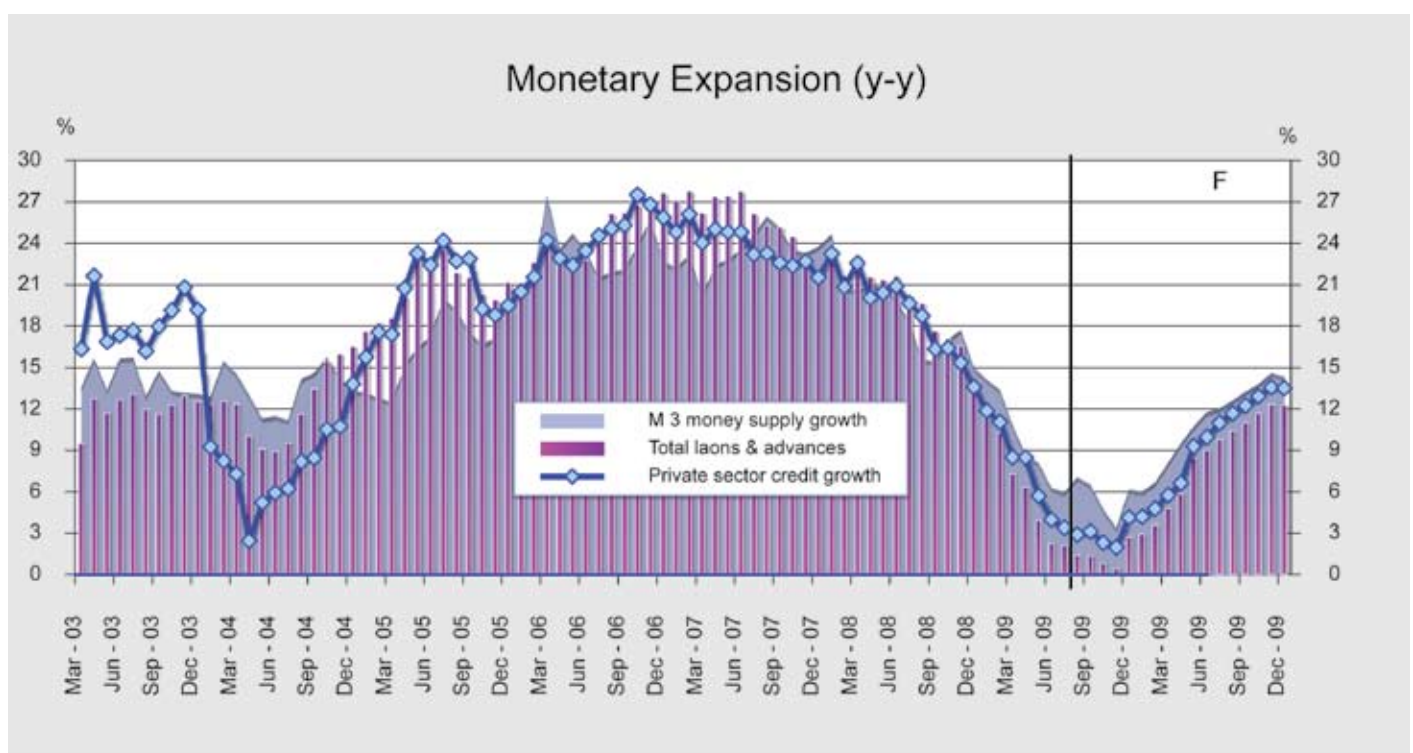
For 2010 the modest economic growth rate could have a marginal positive influence on the business environment. South Africa will still have a high jobless rate but some skilled workers who have been retrenched, could be part of the workforce again. No dramatic improvements can be expected but there will be some relief after a severe

recession. At least it seems as if the bleeding will stop in 2010.

*\*Meyer was a reputable freelance financial journalist and analyst. He passed away on 20 October after a short illness. This is the last of his regular contributions to the FSB Bulletin. Our condolences to his family and friends – Editor.*

### July '09 monetary aggregates key facts:

- M3 money supply growth down to 5.78% (year-on-year) from revised 6.07% in June '09 (was 6.04%).
- Growth in credit extension to the domestic private sector (PSCE) down to 3.40% from 3.98%.
- Growth in total loans and advances (TLA-PSCE growth excluding investments and bills discounted) down to 2.07% from 2.22%.
- Momentum (quarter-on-quarter, seasonally adjusted and annualized – q-q saar): PSCE momentum decelerated to -0.26% from +1.66%. Acceleration in contraction momentum in TLA's to -2.42% from -1.84% and acceleration in momentum in case of M3 to +1.28% from -1.40%.
- Implication for interest rates: Risk of stagflation complicating future interest rate decisions.
- Preliminary year-on-year growth forecast for Aug. '09: M3 6.84%, PSCE 2.89% and TLA 1.42%.



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