national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

MEDIA STATEMENT

DRAFT REGULATIONS DEALING WITH COMMISSION STRUCTURES AND MINIMUM VALUE PROTECTION FOR CONTRACTUAL SAVINGS PRODUCTS OF THE LIFE INSURANCE INDUSTRY

The National Treasury today released for comment draft regulations in terms of the Long Term Insurance Act, 1998, dealing with revised commission structures and enhanced consumer protection for contractual savings products of the life insurance industry.

The regulations follow extensive consultation on the 2006 National Treasury discussion paper, *Contractual Savings in the Life Insurance Industry*, which outlined a range of proposals designed to give effect to the December 2005 Statement of Intent ("SOI") signed between the Minister of Finance and the life insurance industry, aimed at improving the value provided by contractual savings products, such as retirement annuities and endowment policies.

Regulations implemented on 1 December 2006 gave effect to the first phase of the SOI commitments, which encompassed *retrospective* measures to improve policyholder value for policies written in the past and existing policies.

The regulations released today form the next phase of the SOI, designed to further improve the cost effectiveness and consumer protection provided by contractual savings products written in the *future*. These reforms deal specifically with changes to the structure of commission payable on these products, as well as enhanced minimum early termination values.

Commission regulations

Existing intermediary remuneration for contractual savings products is strongly biased in favour of up-front commission, with three-quarters payable in the first year of the policy term and the balance in the second. This reduces the incentive for intermediaries to provide ongoing service and advice to the client and puts at risk the value that policyholders receive, especially in the event of an early termination of the policy.

With this in mind, commission regulations are to be modified to improve the alignment of customer and intermediary interests, including:

- a maximum rate of commission of 5% of premium, of which no more than half may be paid up-front;
- an increase from 2 years to 5 years in the period during which commission payments will be reversed, should a policy be terminated, to act as a disincentive against intermediary mis-selling;
- a provision that policyholders may redirect the payment of commission to another suitably accredited intermediary or insurer representative of their choice, should they be dissatisfied with the level of financial advice and administration they are receiving; and
- a prohibition on the payment of up-front commission if an existing contractual savings product is replaced by another such product, to protect against the risk of unnecessary, commission-driven replacement of policies.

Minimum early termination values

Minimum early termination values are necessary to provide a safety-net against extremely poor policy values in the event of early termination.

At the time of the SOI, the National Treasury indicated that the introduction of revised commission regulations would support further enhancements to these minimum early termination values. These include:

- the maximum deductible charge on an early termination is reduced to 15% of the investment value (from the 30%-35% limit that applies to existing policies), reducing to 0% by half-way through the policy term; plus a capped administration charge to cover termination expenses; and
- early termination charges must be clearly disclosed to the prospective client when applying for an investment policy, as well as in the policyholder summary and in annual statements to policyholders or members.

The proposed regulations are the outcome of careful consideration and consultation, including technical analysis of the potential impact on insurers, intermediaries and policyholders. The regulations include special provisions to cater for the business sustainability of small and emerging intermediaries selling low-premium business.

It is anticipated that, in combination, these measures will contribute to a significant improvement in consumer perceptions of the value offered by the savings products of the life insurance industry, particularly with respect to the burden of cost in the event of early termination.

Taking due cognisance of possible changes to system requirements, an implementation date of 1 August 2008 is proposed.

The draft regulations and a paper providing further explanation of the amendments is available on the National Treasury website: www.treasury.gov.za

The closing date for comment is 20 March 2008.

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