IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

(HELD IN JOHANNESBURG)

CASE NO**: PFA/GA/1142/2002/ZC**

In the complaint between:

THOMSON-CSF SOUTH AFRICA PENSION FUND — **Complainant**

and

ALTRON GROUP PENSION FUND — **First Respondent**

ALLIED ELECTRONICS CORPORATION LIMITED — **Second Respondent**

DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT, 24 OF 1956 ("the Act")

INTRODUCTION

[1] The complaint concerns the alleged refusal by the first respondent to transfer proportionate shares of guarantee reserve relating to future costs and risk reserve in respect of 267 members that were transferred from it to the complainant.

[2] The complaint was received by this office of 29 August 2002. Having considered the written submissions before this tribunal, it is considered unnecessary to hold a hearing in this matter. As the background facts are well known to the parties, only those facts that are pertinent to the issues raised herein shall be repeated. The determination and reasons therefore appear below.

BACKGROUND FACTS ON THE COMPLAINT

[3] This is a re-lodged complaint following my predecessor's, Mr V Ngalwana's, determination dated 13 December 2004, wherein, he ruled that he had no jurisdiction on grounds that the Registrar of pension funds had considered the scheme in terms of section 14 of the Act and found it to be reasonable and equitable and in accordance with the provisions therein.

[4] When he made that ruling in December 2004, he had before him a certificate from the Financial Services Board dated 17 March 2004, which stated:

"**TO WHOM IT MAY CONCERN**

It is hereby certified in terms of section 14(1)(e) of The Pension Funds Act, No 24 of 1956, that the requirements referred to in paragraph (a) to (d) of the above section with regard to the transfer of business with effect from 29 February 200 of 267 members from the ALTRON GROUP PENSION FUND to the THOMSON-CSF SOUTH AFRICA PENSION FUND have been satisfied."

[5] On 5 May 2005 my assistant, Mr M Ramabulana, who originally investigated the complaint, received an e-mail to which was attached a letter dated 25 April 2005 from the Financial Services Board authored by Mr. A. Raphahlela, which states:

"**Transfer of business from the Altron Group Pension Fund (12/8/3720) to the Thomson-CSF SA Pension Fund (12/8/36483) (Case 89220)**

Persuant to this morning's meeting at the financial services Board with your Ms Theresa Clegg and Mr Schalk Burger, I wish to confirm as follows:

1. A certificate to transfer 267 members from the Altron Group Pension Fund to the Thomson-CSF SA Pension Fund (Case 89220) with effect from 29 February 2000, was issued by the Registrar of Pension Funds on 17th March 2004.

2. In considering the application, it was noted that the transfer would not at this stage include shares of the guarantee and risk reserves.

3. The reason for the exclusion of the risk and guarantee reserves was that a dispute was pending before the Pension Funds Adjudicator.

4. I wish to confirm that the Registrar is unable to consider the transfer of these reserve

accounts, until such time as the dispute has been determined by the Pension Funds Adjudicator, or the parties involved have come to some agreement."

[6] This information was not part of our file when my predecessor issued the determination. My predecessor accordingly issue determinations based on the information provided, the certificate as received did not stipulate conditions as contained above. It will not take the matter any further to apportion blame on who bears the responsibility for the miscommunication, safe to say, it is in the best interest of the members of the two parties that this matter be resolved urgently. It follows therefore, that since the reasons which precluded my jurisdiction have actually never been there, I should determine the matter on the merits.

FACTUAL BACKGROUND

[7] Other parties not involved in this dispute but who play a part in the unfolding of the events leading to this dispute are: Thomson-CSF (Pty) Limited ("Thomson-CSF"), African Defence Systems (Pty) Limited ("ADS") and Allied Technologies Limited ("Altech").

[8] My understanding of the events as they unfolded is as follows. ADS was the participating employer in the first respondent. ADS was owned in a 50/50 share split by Altech and Thomson-CSF. Altech is a subsidiary of the second respondent.

[9] From 1 September 1996 the first respondent converted from a defined benefit

("DB") arrangement to a defined contribution ("DC") arrangement. At some point thereafter Thomson-CSF purchased the remaining Altech shares in ADS. It was this agreement that necessitated the transfer of 267 members from the first respondent to the complainant.

[10] During the conversion from a DB to a DC arrangement of the first respondent, members who were contributing before the conversion were given the option to choose whether they wanted to remain in the DB fund or to transfer to the DC fund. It appears that the decision to excise this option could be deferred until member decides to retire. To encourage members to transfer to the DC they were given a guarantee that they were not going to be worse-off at retirement than if they had remained with the DB. To give effect to this promise a guarantee reserve account was created as part of the reserve account.

[11] The reserve account also constituted the risk reserve account which its duty was to cover excesses in death and disability benefits which could not be covered by the member's share. The reserve account constituted the guarantee reserve, the risk reserve, the equalization reserve and the asset reserve.

COMPLAINT

[12] The complainant submits that during the share allocation preceding the section 14 application to transfer the 267 members to it, the first respondent offered to transfer a portion of the guarantee reserve, namely, only in relation to past service.

[13] The complainant alleges that the first respondent is refusing to transfer proportionate shares of:

[13.1] the guarantee reserve relating to future costs; and

[13.2] the risk reserve.

[14] The complainant's complaint is that the 267 members subsequently transferred to it are entitled to proportionate shares of both the guarantee reserve, in relation to future costs, as well as the risk reserves.

[15] In support of the complainant's argument it makes the following submissions.

[15.1] That Mr. Hunter, an actuary who made submissions to the principal officer of the first respondent that the provision made to transfer R1, 07 million for the transferred members will result in a profit to the first respondent to the prejudice of the transferred members, which he concludes is not an equitable transfer as is required by section 14 of the Act.

[15.2] Mr. Hunter opined that the reason why the first respondent's calculations for the allocation of the guarantee reserve were incorrect was that old salary scales were used instead of the new salary scales in existence at the time of the calculation.

[15.3] The complainant also relied on Mr. Southey's argument, another actuary who

made submissions to the Registrar of Pension Funds that the guarantee reserve to be transferred as proposed only covered the transferred members' past service, while it is supposed to cover future benefits as part and parcel of members reasonable benefit expectations. Mr. Southey concurs with Mr. Hunter on the issue of salary scales used. He states that the salary scales used were 14 months old and failed to consider the increase.

[15.4] As far as the risk reserve is concerned Mr. Southey opined that this reserve is for the direct benefit of members. He argues that as the complainant is not self-insured the transferred members' contributions will include a risk premium which leaves them worse-off than their remaining counterparts.

[15.5] The complainant argue further that a third actuary, Mr Gluckman, confirms the two opinions and submits that an equitable transfer of the guarantee reserve and the risk reserve can only be achieved through a proportional share of these reserves.

[16] The complainant seeks relief in the form of a proportional share for the 267 members transferred to it of:

[16.1] the guarantee reserve, including future costs; and

[16.2] the risk reserve.

RESPONSE

[17] The Respondents, through their attorneys Brink Cohen Le Roux and Roodt Inc. gave a comprehensive response to the issue raised in the complaint. They confirmed and agreed with the background facts.

[18] In regard to why it only transferred a share of past guarantee reserve they allege that:

[18.1] this provision covers those employees who were members of the first respondent before the conversion in case they elect to be paid in terms DB rules. Furthermore, if a member retires early the retirement benefit will not be based on contributions made until the normal retirement age;

[18.2] In the first respondent's experience most of their member do not remain with Altech until retirement;

[18.3] that transfer value should only take into account past service as this is the benefit that has vested;

[18.4] unless the complainant established a similar fund for the transferred members, there is no proof that they are going to be worse-off at retirement than their remaining counterparts;

[18.5] the reason why the fund relied on old salary scales was that:

(a) they were the salaries applicable at the time, 29 February 2000;

(b) salaries were only increased 3 months after the apportionment date with retrospective effect;

(c) the employer (ADS) and the new fund (the complainant) failed to inform first respondent of the new changes until there was already a dispute; and

(d) even if the increased salaries had been considered, funds would have had to be transferred from the investment reserve to the guaranteed reserve.

[19] In regard to why the first respondent refused to share the risk reserve it alleges that:

[19.1] there are indications that its membership may increase which will make demand that the risk reserve will have to be increased; and

[19.2] the risk reserve constitutes an indirect benefit to members, therefore if it were to be transferred to members' share accounts it will be providing them with a direct benefit which they did not enjoy before transfer and also not enjoyed by the non-transferring members.

[20] The first respondent argues that it was these considerations together with the advice from its actuaries and the provisions in its rules that motivated its decisions

not to share the risk reserve and to only share past service related part of the guarantee reserve. It submits that its apportionment (or non-apportionment in regard to the risk reserve) was the most equitable under the circumstances.

DETERMINATION AND REASONS THEREFOR

[21] The parties are in agreement as to issues in dispute, it is the conclusions reached that separates their respective views. Both sides also appear to rely on expert advice contained in attached opinions in reaching their different conclusions. The complainant's complaint is that the share distribution, in particular relating to the guarantee reserve and the risk reserve, failed to comply with the provisions of section 14 of the Act.

[22] Section 14 of the Act provides how amalgamations and transfers of members from one fund to another are to be carried out and it reads:

> "(1) No transaction involving the amalgamation of any business carried on by a registered fund with any business carried on by any other person (irrespective of whether that other person is or is not a registered fund), or the transfer of any business from a registered fund to any other person, or the transfer of any business from any other person to a registered fund shall be of any force or effect unless-
>
> (a) the scheme for the proposed transaction, including a copy of every actuarial or other statement taken into account for the purposes of the scheme, has been submitted to the registrar;

(b) the registrar has been furnished with such additional particulars or such a special report by a valuator, as he may deem necessary for the purpose of this subsection;

(c) the registrar is satisfied that the scheme referred to in paragraph (a) is reasonable and equitable and accords full recognition-

(i) to the rights and reasonable benefit expectations of the members transferring in terms of the rules of the fund where such rights and reasonable benefit expectations relate to the service prior to the date of transfer;

(ii) to any additional benefits in respect of service prior to the date of transfer , the payment of which has become established practice; and

(iii) to the payment of minimum benefits referred in section 14A,

and that the proposed transactions would not render any fund which is a party thereto and which will continue to exist if the proposed transaction is completed, unable to meet the requirements of this Act or to remain in sound financial condition or, in the case of a fund which is not in a sound financial condition, to attain such a condition within a period of time deemed by the registrar to be satisfactory."

[23] Rule 2.2(4) of the first respondent's rules provide the reason behind the guarantee reserve and it states:

"The purpose of the guarantee reserve is to provide for the additional cost of benefits to which a MEMBER may become entitled should he elect to receive the benefits in terms of the OLD RULES in accordance with the provisions of appendix B. The amount required in the guarantee reserve shall be determined by the ACTUARY on a basis approved by the TRUSTEES. The following transactions shall be recorded in the guarantee reserve:

(a) Credits

(i) an opening balance as calculated by the ACTUARY as at the CONVERSION DATE on a basis approved by the TRUSTEES;

(ii) investment declarations transferred from the asset reserve at the same rate as that referred to in Rule 2.2(1)(a)(v);

(iii) amounts transferred from the asset or other reserves in the event of a shortfall to meet the accrued liabilities when read in conjunction with Rules 10.9(3) and 10.9.(4), the amount of which shall be calculated by the ACTUARY and APPROVED by the TRUSTEES;

(iv) amounts transferred from the Share Account in terms of Rule 2.2(1)(b)(vii).

(b) Debits

(i) transfers to the Share Account in terms of Rule 2.2(1)(a)(vi);

(ii) ad hoc transfers to the Pensions Account in terms of Rule 2.2(2)(a)(v);

(iii) amounts transferred to the asset reserve in the event of a negative declaration by the TRUSTEES in terms of the provision of Rule 2.2(4)(a)(ii);

(iv) amounts transferred to the asset reserve or risk reserve in the event of a MEMBER entitled to select a benefits payable under the OLD RULES (as contemplated in appendix B) chooses not to do so, the amount of which shall be calculated by the ACTUARY on a basis approved by the TRUSTEES.

[24] Rule 2.2(7) of the first respondent's rules provide the reason behind the risk reserve and it states:

"The primary purpose of the risk reserve is to provide for future death benefit payments in excess of those covered by the deceased MEMBER'S SHARE and to cover the cost of disability benefits. The risk reserve is also intended to meet the expenses related to management and administration of the FUND. In addition it may be used to meet other adverse contingencies:

(a) Credits

(i) an opening balance as determined by the TRUSTEES after consultation with the ACTUARY as at the CONVERSION DATE;

(ii) the EMPLOYER'S contributions made after the CONVERSION DATE in terms of Rule 8.2(3);

(iii) any reinsurance payments made to the FUND by an INSURER;

(iv) investment declaration transferred from the asset reserve as at the same rate as that referred to in Rule 2.2.(1)(a)(v);

(v) amounts transferred from the Pensions Account in terms of Rule 2.2.(2)(b)(vi);

(vi) MEMBER'S contributions as set out in Rule 8.1(1)(b).

(b) Debits

(i) transfers to the Share Account in terms of Rule 2.2(1)(a)(vii);

(ii) amounts transferred to the asset reserve in the event of a negative investment declaration by the TRUSTEES in terms of the provisions of Rule 2.2(7)(a)(iv);

(iii) reinsurance premiums referred to in Rule 9.3;

(iv) all costs and expenses referred to in Rule 10.15;

(v) amount transferred to the Pensions Account in terms of Rule 2.2(2)(a)(v);

(vi) any cost arising from data errors.

[25] Section 14 demands that the Registrar is satisfied that the fund's transferring members':

[25.1] rights and reasonable benefit expectations of transferring members in terms of the rules of a fund were such rights and reasonable benefit expectations relate to their service prior to date of transfer are accorded full recognition;

[25.2] (any) additional benefit in respect of service prior to date of transfer, the payment of which has become established practice is accorded full recognition; and

[25.3] payment of minimum benefit as required in section 14A is accorded full recognition.

[26] These requirements should be checked with the condition that the proposed transfer will not render both the transferor and the transferee funds, unable to meet the requirement of this Act or to remain in a sound financial position. If it does, that such financial condition will be addressed in a time which the registrar deems reasonable.

Sharing of Risk Reserve

[27] I shall deal first with the risk reserve since the first respondent is refusing to share in it in its entirety. The purpose of the risk reserve is as stipulated in rule 2.2(7) above. It is clear from this rule that it serves as an insurance policy against unforeseen specified contingencies, which the fund calls self-insurance. The argument of the first respondent is that we cannot share this reserve since the complainant does not provide an equivalent self-insurance. This has the unfortunate results that the transferred member loses out on this benefit.

[28] However, this argument does not hold water since the transferred members still have to be insured for those contingencies that this risk reserve is meant to cover. The first respondent does note in its argument that it may have to contribute more money to this risk reserve even after deciding not share in it, due to rising demand. What surprises me is that recognizing this burden on the first respondent and its duty to cater for it, it fails to recognize the same for the complainant towards the transferred members. Thus in my understanding of putting the transferred members in as good a position as the remaining ones, it is only fair that a proportionate portion of this reserve be transferred for that particular purpose.

[29] The argument that the complainant is not self insured, therefore, it is not entitled to the risk reserve cannot be sustained in that, it does not eliminate the transferred members' need to the risk cover. Thus, the transferred members will bear the burden themselves to enjoy the same benefits.

[30] This transferred members had a reasonable expectation prior to transfer to share in this benefit, which they have subsequently been denied. There are no allegations that the first respondent will be unable to comply with its duties in terms of the Act, or that it will not be in a sound financial position. The worst case scenario for the first respondent on its version is that the investment reserve (crediting fund) will be depleted.

[31] I am therefore not persuaded by the first respondent's argument that the risk reserve should not be proportionally shared with the transferred members.

Sharing of Guarantee Reserve

[32] In regard to the distribution of the guarantee reserve, the first respondent avers that the reason as to why the old salary scales were used and not the new ones is that the salaries were declared with retrospective effect and it was not informed on time.

[33] This reasoning is flawed in that the time alone it took for this matter to be resolved (from 2000 when the attempt to the negotiations started to transfer), far outweighs in proportions the effort to recalculate the updated salary values. Of paramount importance is the interest of the members to be treated fairly by the scheme, which in my opinion would entitle the members to be transferred to point out any inequities in the scheme at any point before the transfer is made. I also do not agree with the logic that a retrospective salary increase only influence the pension status of the

members from the actual date of increase (see *Bohm v National Productivity Institute and Another* [2005] 3 BPLR 253 (PFA).

[34] The first respondent also submits that the guarantee reserve is only applicable to past service since that is the only benefit which has vested. I battle to find the logic of the first respondent's argument in support of its view in this respect. It argues that this benefit is conditional for its members who may choose to retire in terms of the DB rules and this is in its experience a common trend. From this it concludes that the transfer value should only take into consideration values that have accrued which is only past values.

[35] I fail to see the link between the assertion made and the conclusion reached. My understanding is that this guarantee reserve is a conditional provision, meaning, <u>if in future</u>, a member decides to elect to retire by the DB rules he will get the benefit. As to how this excludes the transfer of future benefits for the transferred members is not explained. On the first respondent's own argument it admits that the complainant were to establish a similar fund then it will be entitled to share on the prospective benefits from this guarantee fund. This negates the argument that this benefits are only limited to the past and confirms the argument that a value (past and future) is due which must be shared with the transferred members.

[36] The first respondent argues further that the complainant's insistence that the transferred members should not be made worse off as a result of the transfer cannot be guaranteed by "the payment of appropriate amounts into the members'

share accounts in the complainant does not necessarily have the result that they will not be worse of at retirement." This argument is disingenuous in that the best way to determine whether the transferred members are to be worse of at retirement starts at transfer stage. Any deductions made as to how the transferred members are to fair at retirement will stand and fall on the share they received in comparison to their counterparts who did not transfer.

[37] Similarly, I am not convinced of the reasonable benefit expectation of the members prior to the transfer in regard to the guarantee reserve have been met. The reasons proffered by the first respondent as to why it refuses to share proportionally the future values of the guarantee reserve do not address the members' reasonable expectations, nor do they protect the first respondent from failing to meet it financial obligations as is required by the Act.

[38] In the result, both complaints by the complainant against the first respondent succeeds.

RELIEF

[39] In the result, the order of this Tribunal is as follows:

[39.1] The first respondent is ordered to calculate within 4 weeks from the date of this determination the proportional share of the guarantee sub-reserve (R85 103 000,00) in relation to past and future costs, taking into consideration the

retrospective salary increase applicable from 1 January 2000, for the 267 members transferred to the complainant as at 29 February 2000.

[39.2] The first respondent is ordered to calculate within 4 weeks from the date of this determination the proportional share of the risk sub-reserve (18 718 000, 00), taking into consideration the retrospective salary increase applicable from 1 January 2000, for the 267 members transferred to the complainant as at 29 February 2000.

[39.3] The first respondent is ordered to lodge an application in terms of section 14 of the Act, with the Registrar of Pension Funds, for the transfer to the complainant, of the guarantee sub-reserve and the risk sub-reserve accounts as determined in paragraphs [39.1] and [39.2] respectively, together with interest earned from 29 February 2000.

DATED AT JOHANNESBURG ON THIS DAY OF 2008.

Yours faithfully

MAMODUPI MOHLALA
PENSION FUNDS ADJUDICATOR