IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO.:PFA/GA/153/98/JM

In the complaint between:

Younghusband and Others — Complainant

and

Decca Contractors (South Africa) Pension Fund and its Trustees — Respondent

---

DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT OF 1956

Introduction:

This is a complaint lodged with the Pension Funds Adjudicator in terms of section 30A(3) in terms of the Pension Funds Act of 1956.

The complainants seek an order directing the trustees of the pension fund to transfer to the Superflex Pension Fund the complainant's actuarial reserve values, together with a portion of the surplus in the fund, in accordance with guidelines to be determined.

The complainants are identified in the complaint and are former members of the respondent, making up approximately 60% of the active membership of the fund at the time of the termination of their membership.

The respondent fund is a defined benefit pension fund registered under the Pension Funds Act of 1956. The fund is funded by employee contributions of 7.5% of pensionable salaries. The employer contribution is the balance of cost, as recommended by their actuaries in consultation with the trustees, to fund the benefits in terms of rule 19.1 of its rules.

On 19 May 1998, under cover of a letter dated 18 May 1998, the complainants lodged a complaint with the office of the Pension Funds Adjudicator. On 7 July 1998 a letter was addressed to the trustees of the respondent affording them 21 days in which to respond to the complaint. The respondent failed to comply with this direction. Subsequent attempts to elicit a written response from the respondents also proved unsuccessful. Eventually, towards the end of January 1999, the legal representatives of the parties agreed to a statement of facts replacing the statement of facts filed with the original complaint and the matter was set down for a hearing on 4 February 1999. At the hearing, the legal representatives of the complainant filed comprehensive heads of argument in support of the relief sought. The respondent's legal representative advanced oral argument at the hearing. Subsequent to the hearing there was disagreement concerning an alleged undertaking by the respondent's legal representative to furnish heads of argument. The respondent's legal representative took the view that heads of argument would only be appropriate after the hearing of further evidence. However, after further correspondence, on 24 March 1999, the respondent's legal representative eventually filed heads or argument. This determination, therefore, is based upon the documentation filed and the agreed statement of facts, together with the written and oral submissions made during and subsequent to the hearing.

The complainants were represented by Mr C Jonker of Edward, Nathan & Friedland. The respondents were represented by Dr K Douglas of Webber, Wentzel Bowens.

Having completed my investigation, and having decided to determine the complaint as follows, these are my reasons.

The facts

The following facts, derived principally from the agreed statement of facts and supporting documentation, are common cause.

On 27 February 1997, Litton Industries Inc ("LMS") purchased the assets and business of Racal Electronics (South Africa) (Pty) Ltd ("Racal SA"), previously known as Decca (South Africa) (Pty) Ltd. Racal SA is the only participating employer in the respondent pension fund. The purchase of the assets and business of a division of Racal SA, was part of a world wide purchase by LMS from Racal Electronics Plc of the United Kingdom ("Racal UK"). The purchase was with effect from 1 March 1997 ("the completion date").
In terms of section 197(2)(a) of the Labour Relations Act 66 of 1995 all the rights and obligations between Racal SA and the employees employed in the business sold, constituting approximately 60% of the active members of the fund, continued in force as if they were rights and obligations between LMS and the employees.

LMS did not have its own pension fund and wished to establish its own pension arrangements for the transferring members. It accordingly retained Ginsburg Malan & Carsons, Actuaries, to do so, which they did in the form of an umbrella fund, the Superflex Fund, of which LMS become a participating employer. The fund is a defined contribution fund and the benefit payable in respect of a member is accordingly based on the contributions paid in respect of the member plus the investment return on the contributions. The fund offers a choice of investment media from market-related portfolios to cash or near cash portfolios.

While LMS was making its new pension arrangements for the transferring members, Racal UK and Racal SA (together "Racal") and the Decca Fund accommodated LMS by agreeing that the Decca fund would continue to accept contributions in respect of the transferring members in the interim. The rules of Decca Fund however had not, and have not, been amended to admit LMS as a participating employer and hence to enable the transferring members to remain members. This continued until 31 March 1998 when Racal and the Decca Fund notified LMS that they were no longer prepared to continue this

"irregular situation". No further contributions were accepted by the Decca Fund in respect of the transferring members after that. The transferring members became members of the Superflex Fund on 1 April 1998.

In the meantime a difference of opinion emerged between Racal and LMS as to the proper basis for the calculation of the amount transferable in respect of the transferring members. Racal took the view that the amount in respect of each member was the actuarial liability in respect of the member while LMS took the view that a proportionate share of the surplus including the investment reserve was also transferable.

The 31 March 1994 actuarial valuation of the Decca Fund had shown a significant surplus of assets over accrued liabilities. Racal SA subsequently decided, with the approval of the actuaries and the trustees, to suspend its contributions to the Decca Fund (which contributions, disregarding the surplus, would have been approximately 7.5% of pensionable salaries according to the valuation) until the 1997 actuarial valuation when the Decca Fund would again be actuarially assessed. During the period when the employer was on "contribution holiday", ie from 1 November 1994 to 30 June 1996, the employees continued to contribute normally.

The actuarial valuation as at the completion date, comparing the value of the assets with the value of the benefits accrued to the valuation date with allowance for future salary increases, reveals that the fund was in surplus. The surplus excluding the investment reserve was R2 219 000 made up as follows:

R8 510 000	-	"actuarial value" of assets
R6 291 000	-	accrued liabilities
R2 219 000		

This gave a funding level of 135.27%.

The “actuarial value” of the assets was a discounted value recommended by the actuary to provide a cushion in case investment values should decrease, known as an “investment reserve”. The amount of the investment reserve in the case of the fund was R1 239 863 made up as follows:

R9 428 619	-	“Actuarial value” of R8 188 756 in respect of insurance company investments) 0,8685 being the discount factor used by the actuary
R 258 686	-	cash
R 63 030	-	sundry debtors less sundry creditors
R9 750 335	-	market value of assets
R8 510 472	-	actuarial value of assets
R1 239 863	-	investment reserve

The total surplus in the fund including the investment reserve was therefore R3 458 863 made up as follows:

R1 239 863	-	investment reserve
R2 219 000	-	other surplus
R3 458 863		

This translates to a funding level of 155%.

In his valuation, the actuary also considers the financial position of the fund allowing for future benefits and normal contributions. On the basis the liabilities increase to R8 361 000 and the surplus of R1 388 863 is made up as follows:

R1 239 863	-	investment reserve

R 149 000	-	remainder of surplus
R1 388 863		

This translates to a funding level of 116.5%.

In terms of clause 18 of the purchase agreement, pensions of transferring employees are required to be dealt with in accordance with the provisions of schedule 9 of the agreement. Schedule 9 is made up of two parts. Part 1 deals with pensions in the United Kingdom. Part 2 deals with pensions in relation to those companies in other parts of the world. The schedule consists of two clauses which read as follows:

1. Definition

In this Part 2 of this Schedule "Pension Plan" shall mean the following arrangements of the Vendors for the provision of retirement and other benefits to any Employees, details of which are set out in the Disclosure Letter:

Canada	Retirement Income Plan for employees of R-DCL, part of the Racal-Chubb Retirement Income plan;
Denmark	R-DD Retirement, Survivors and Disability Plan;
Sweden	ITP (mandatory defined benefit plan);
South Africa	Decca Contractors (SA) Pension Fund;
The Netherlands	Defined benefit plan insured with Delta Lloyd Insurance Company;

2. Transfer

2.1 In consideration of Litton's undertaking in paragraph 2.3 below, Racal shall or shall procure that the Vendors shall, with effect from the Completion

Date, transfer to Litton the Pension Plans together with all rights, duties and obligations attaching to them.

2.2 In respect of South Africa sufficient assets will be made available to fully cover liabilities accrued at the Completion Date, with allowance for future salary increases on the basis that this will be transferred to individual or collective pension arrangements for the transferring employees.

2.3 Litton shall with effect from the Completion Date assume all liabilities arising under or in connection with the Pension Plans.

The rules of the Decca Fund do not expressly provide options for members whose contracts of employment are assigned or transferred in terms of section 197 of the Labour Relations Act. However, rule 29.1 grants certain options to members whose employment has been terminated by resignation or dismissal. The rule provides that members may elect to transfer to another fund, to take the benefit in cash or to retain the benefit in the Decca Fund, and if a member does not make an election within the 31 days he or she is deemed to have elected to take the benefit in cash.

Ginsburg Malan & Carsons, acting on behalf of LMS, in response to Racal's attitude about the quantum of the transfer values, addressed a letter to the Decca Fund, dated 6 November 1997, stating that they could not advise acceptance of the proposed transfer to the Superflex Fund consisting only of members' actuarial reserve, for a variety of reasons.

In his response dated 10 February 1998, Mr Talbot (the principal officer of the fund) stated *inter alia* that the sale and purchase agreement referred to "sufficient assets to fully cover the liabilities", whereas what was being proposed by LMS's actuaries was an amount in excess of these liabilities. He added that if Racal were to adhere precisely to the wording of the sale and purchase agreement, the liabilities would be based on benefits calculated at the completion date and not at the transfer date. This letter was written in his capacity as financial manager of Racal SA.

At a meeting of the trustees of the Decca Fund held on 26 February 1998, the trustees received a presentation from Mr S Peile of Alexander Forbes, the Decca Fund's administrators, on the issues he considered relevant to the amount that should be transferred in respect of the transferring members. The majority of the trustees then resolved that the transfer of the actuarial reserves plus a share of the investment reserve would be reasonable and a sound basis to transfer assets of the new LMS fund and would accurately reflect the intention of the sale and purchase agreement. None of the trustees was however a party to the agreement or the negotiations giving rise to it and they were mistaken as to the parties' intention which was to transfer assets having a market value equal to the actuarial liabilities only. The minutes of the meeting also refer to the trustees having adopted a rule amendment tabled at the meeting to give effect to their resolution. The tabled amendment and the registration of the rule amendment was not proceeded with, for reasons not clear. The relevant minute (clause 4) is worth repeating in full. It reads:-

> Sale of Racal Marine to Litton Group
>
> Mr Peile tabled a letter from the consultants to the Litton Group, Ginsburg, Malan & Carsons as well as a reply by Mr Talbot in his capacity as Financial Manager of Decca (SA) (Pty) Ltd.
>
> Mr Peile explained the salient points for consideration by the trustees:
>
> 1. In terms of the sale agreement, the new Litton fund is to be a mirror image of the existing Decca Contractors (SA) Pension Fund. In terms of the sale agreement, sufficient assets
>
> must be transferred to the new fund in order to fully cover the liabilities accrued in that fund. The calculation of transfer values on the valuation basis excluding an investment reserve could render the new fund financially unsound from inception. However, a transfer of reserve values grossed up to include the investment reserve would ensure that the new fund has sufficient assets to cover its accrued liabilities.

Mr Peile advised the trustees that it is the practice of the Financial Services Board to not allow the transfer of actuarial reserve only from a defined benefit fund which is in a surplus position, where the valuator determined that an investment reserve is necessary.

The trustees must endeavour do give effect to the terms of the purchase and sale agreement while at the same time satisfying themselves that neither fund is placed in an unsound financial condition. The purchase and sale agreement in itself does not make reference to a transfer of surplus the purchase price could be renegotiated to reflect the purchase of that surplus. It was confirmed that there was no such enhancement reflected in the sale price.

2. There is currently no provision in the rules of the Decca Contractors (SA) Pension Fund to give effect to the terms of the purchase and sale agreement and accordingly an amendment has been drafted to give effect to the terms of this agreement. There is a rule currently in the Pension Fund rules pertaining to takeovers and or amalgamations which does not relate to the circumstances of this sale.

3. The question of members reasonable benefit expectations as per the Financial Services Board guidelines have been met by virtue of the fact that transfer values include the allowances deemed necessary by the valuator to allow for future salary increases and pension increases.

4. The issue of whether the TEK case has particular relevance to this situation was also canvassed by Mr Peile and in light of the fact that the TEK case dealt with a particular set of circumstances which are not applicable to this fund it was agreed as such that the TEK case was of no direct relevance to this situation. Mr Peile explained to the trustees that the point that should be considered by the trustees, as a

result of the TEK case, was how the current surplus situation had arisen. Mr Peile advised the trustees that in his opinion it would be reasonable to conclude that the surplus had arisen as a result of historic over
contributions by the employer due to the assumptions being made by the valuator in determining the employer's contribution rate being shown by subsequent experience to have been too conservative.

5. Mr Peile stated further that the basis for transfer to the Litton Fund must be that as adopted by the valuator of the Decca Contractors (SA) Pension Fund and must be in terms of the basis used by the valuator in the latest valuation of the fund. To utilise a different basis would have no sound basis. Of course should the valuator of the transferee fund utilise a different basis for valuing the assets there could well be a deficit in the new fund. There is no requirement under the Pension Funds Act or any other legislation to the effect that the transferee fund should be 100% funded on the transferee funds' valuator's assumptions.

6. On the basis of the above decision, the trustees with the exception of Mr Tanneberger agreed that the transfer of actuarial reserve including the investment reserve is a reasonable and sound basis to transfer assets to the new Litton Fund and would accurately reflect the intention of the purchase and sale agreement while not prejudicing the transferring members by virtue of the fact that they would be ensured that their fund was in a sound financial condition based on the transferor funds valuation assumptions.

It was agreed by following trustees that the amendment be approved:

Mr A J Bothwick
Mr B K Talbot
Mr R Sommerville

Mr Tanneberger requested that his dissenting vote be reflected by the following:

"I am of the opinion that the additional rule 46 is inequitable to the Litton employees with regards to the transfer of assets to the new Litton arrangements. Not only is the new Rule 46 designed to have retrospective effect (from 1 August 1997) but also creates a conflict with the benefits on "takeover" i.e. rule 35 which specifically includes an appropriate proportion of any revealed actuarial surplus.

As you are aware Litton will be submitting a dispute with the pension funds adjudicator and
its again only seems equitable to await his ruling before amending the pension fund rules. I believe there is no doubt that the pension fund adjudicator will see this proposed rule amendment in poor light in terms of the dispute."

Two letters from Mr L Hammond (senior solicitor of Racal UK) dated 12 and 20 March 2998 respectively, addressed to Mr W von Kumberg (Legal Advisor to Litton Corporation Law Department Europe) were received in response to LMS concerns about the transfer values.

In the letter dated 12 March, Mr Hammond reiterated that Racal maintained its position of offering a transfer on the basis of past service actuarial reserve. It is stated that as LMS had subsequently taken the approach of claiming that transfer should take place on a basis which was neither agreed to nor one that the relevant members are entitled to. Moreover, Racal was at the time of the opinion that it had no option but to take the following action to conclude the matter:

(a) The transferring members would cease to accrue benefits in the fund with effect from 31 March 1998 and no further contributions would be accepted after that date.

(b) The past service actuarial reserve for each active LMS member would need to be calculated. Option forms would be given to the transferring members so that they could elect whether to transfer their benefits to the Superflex Fund or to an individual arrangement or to elect to remain a "preserved" member of the Decca Fund. The members would be given one month, from the date of being advised of the amount of their transfer value, in which to make the election.

(c) Racal offered to LMS to make a joint announcement to the transferring members regarding the position and requested details of the LMS scheme to enable it to prepare the announcement.

In Mr Hammond's letter dated 20 March, he stated that as far as Racal was concerned, there was no dispute as to the calculation of the transfer value. Under the terms of the sale and purchase agreement, Racal had agreed that "sufficient assets would be made

available to fully cover liabilities accrued at completion date, with allowances for future salary increases". This obligation would in Racal's opinion be satisfied by the offer of a transfer value based on each transferring member's past service actuarial reserve. It was further stated that, under the terms of the sale and purchase agreement there is no obligation on Racal to either consult or agree with LMS on the assumptions used in the calculations. The complainants do not pursue the contention that Racal was so obliged.

On 6 April 1998 a letter was addressed to Mr Talbot and the trustees of Decca Fund by the attorneys of LMS, Edward Nathan & Friedland ("ENF"). The letter was in response to Mr Hammond's letters dated 12 and 20 March 1998. The trustees were informed that ENF had advised its client to institute proceedings against the trustees of the Decca Fund on behalf of the members of the Decca Fund in terms of the dispute procedure provided for in section 30 of the Pension Funds

Act; and to lodge a complaint with the Registrar of Pension Funds against the trustees of the Decca Fund, in respect of failure to comply with section 14 of the Pension Funds Act, should the trustees continue with the transfer without following the necessary procedures.

Another letter was sent to the trustees of the Decca Fund dated 9 April 1998 by ENF requesting the trustees to confirm whether they intended to follow the process in terms of Section 14 of the Pension Funds Act and to advise ENF thereof before attempting to execute transfers.

A letter was received from Mr Talbot, on behalf of the trustees, dated 16 April 1998, in which he confirmed that they did intend to follow the process provided for in terms of Section 14 of the Pension Funds Act.

A letter dated 21 April 1998 was sent by ENF to Mr Talbot and the trustees, requesting them to provide ENF with a copy of the application to the Registrar before or on submission thereof, based on the fact that their clients had an interest in the application to be made in terms of section 14.

ENF lodged a complaint with the Pension Funds Adjudicator on 19 May 1998 on behalf of the members of the Decca Pension Fund who were transferred as well as other interested parties.

In a letter dated 2 April 1998, Mr Leeman of Alexander Forbes instructed Clemans, Murfin and Rolland, Consulting Actuaries, to provide updated accrued actuarial reserve values for each transferring member. LMS received the updated schedule of values “excluding investments reserves” on 22 May 1998. In a letter dated 29 May 1998 Clemans Murfin and Rolland confirmed that the figures given to Mr Leeman are the actuarial reserve value for each LMS member with no enhancement for investment reserves.

Although the trustees agreed in the meeting held on 26 February 1998 that the "transfer of actuarial reserve including the investment reserve is a reasonable and sound basis to transfer assets" to the Superflex Fund, Mr Leeman (advisor to the Decca Fund) subsequently informed Mr Elschot (Senior Sales Manager of LMS) that only the actuarial reserve (excluding investment reserve) would be transferred.

An application in terms of section 24 and 25 of the Pension Funds Act was lodged with the Registrar of Pension Funds on 18 June 1998 by ENF requesting an enquiry into the Decca Fund's business and transactions.

The Registrar of Pension Funds replied to the application referred to in paragraph 26 above in a letter dated 25 June 1998. He stated that if the Pension Funds Adjudicator

had already started an investigation, the Financial Services Board must await his findings. If the Adjudicator had not yet started his investigations the Financial Services Board proposed to note on the fund file that any further amendments and any section 14 application should be properly vetted to nullify any irregularities.

In a letter dated 25 June 1998, the local attorneys of Racal, Webber Wentzel Bowens ("WWB") replied to ENF's letter dated 6 April 1998 as follows:

(a) the wording of the sale and purchase agreement precluded a "share of fund" approach;

(b) the transferring members ceased to be members of the Decca Fund on 28 February 1997 when they ceased to be employed by a participating employer and would remain so unless the position was regularised as proposed later in the letter;

(c) Racal and Decca fund had sought to accommodate LMS by *de facto* permitting the

continuation of contributions for over a year in respect of the transferring members but they were not prepared to allow this irregular situation to drag on further;

(d) their clients were willing to extend the 31 day period for the transferring members to exercise their option under rule 29(1);

(e) section 14 has no application because there is no transfer of part or all of the business, ie assets and liabilities, of the Decca Fund; benefits become due and are simply paid by the fund even if individual members elect that payment be made by transfer to the new LMS Fund;

(f) The accrued liabilities in respect of the transferring members could only include

a share of the surplus if such members had a right to that portion of the surplus;

(g) the concept of a surplus at a point in time is purely notional and the notional surplus may be reduced or increased by subsequent market fluctuations, and therefore the transferring members could not have any claim to the surplus. This would give them a vested right in the surplus placing them in a better position than the remaining members;

(h) unless a later date should be agreed on and the rules amended accordingly the only relevant date for the determination of the amounts of the benefits would be 28 February 1997. The contributions paid after that in respect of the transferring members would in principle also be returnable to the payers;

(i) rule 35 is inapplicable - the sale was of assets not a subsidiary;

(j) the *Tek* case turned on quite different facts, is on appeal and is irreconcilable with earlier cases;

(k) their clients stood by the actuarial assumption used by the actuary of the Decca Fund;

(l) the rules of the Decca Fund do not give the trustees the power to consider an apportionment of the surplus and they knew of no implied power to do so on withdrawal of one or more members even if they constitute "a substantial number". A payment of benefits that had become due and payable was in issue, not a transfer;

(m) the proceedings would be defended;

(n) the sale and purchase agreement falls outside the jurisdiction of the Adjudicator;

(o) their clients' proposal to solve the matter was;

(i) the rules be amended with retrospective effect to 1 March 1997 (assuming the Registrar and CIR so agreed):

A. To permit the continued membership of the transferring members from 1 March 1997 to 31 March 1998 and to admit LMS as a participating employer to this extent;

B. To grant the transferring members the enhanced benefits agreed upon in the sale and purchase agreement;

(ii) the liability in respect of each transferring member be calculated at 31 March 1998 (the Decca Fund's year-end) on the same basis as the existing calculation, ie excluding the surplus;

(iii) a joint statement be issued to members explaining the position and giving members

the extended period to exercise the option.

ENF replied to the letter of WWB on 8 July 1998 stating that it was not appropriate to answer the letter in full at the time but reserving the right to do so.

Rule 35, to which WWB refers, deals with takeovers and amalgamation of the employer. The rule essentially provides that in such circumstances the member shall be entitled to a cash sum equal to the total of the actuarial reserve and an amount representing his equitable portion as ascertained by the actuary, of any surplus monies in the fund after

taking into account the actuarial reserve. The relevant portion of the rule reads as follows:

Take over or amalgamation of employer

Notwithstanding the provisions of any other Rule, on the takeover or amalgamation of the Employer by or with any other company or organisation, as from the date of such takeover or amalgamation.

35.1 each Member in the employment of the Employer who has passed his Normal Retirement Date shall be deemed to have retired on that date and will be entitled to an immediate payment of his retirement benefit in accordance with these Rules;

each Member in the employment of the Employer who has not reached his Normal Retirement Date shall be entitled to a cash sum equal to the total of

35.2.1 the actuarial reserve of his pension at the date of takeover or amalgamation, as ascertained by the Actuary in accordance with the basis detailed in the most recent statutory report of the Fund, and

35.2.2 an amount representing his equitable portion, as ascertained by the Actuary, of any surplus moneys in the Fund after taking into account the amount calculated in respect of each Member in terms of rule 35.2.1.

In a letter from Mr Hammond dated 13 August 1998 addressed to W von Kumberg, it was reiterated that the rules of the Decca Fund do not provide for a “bulk transfer” of members’ accrued benefits, as contemplated by the relevant provisions of the sale and purchase agreement, or a transfer of a member’s accrued benefits to another pension fund without the member’s consent.

Racal also indicated that it would not request the trustees to make the loan to the Superflex Fund requested by LMS [its lawyers had advised that the Decca Fund had no power to make loans] but would request the trustees to make payment in accordance with

the rules dealing with options on termination of employment, with an extension of the option period and payment to be without prejudice to the complaint proceedings.

In reply to the letter of Mr Hammond, ENF sent a letter to Mr Talbot and the trustees of the Decca Fund on 19 August 1998. The letter informed the trustees that a substantial number of the members of the Superflex Fund were in the process of being dismissed based on operational requirements. They would therefore, in the near future, be paid the appropriate benefits by the Superflex Fund, failing which they would expose themselves to a claim based on negligence.

LMS continued to request an advance payment to the Superflex Fund and the trustees replied through WWB on 8 September 1998 that they would like to assist , and Racal raised no objection, by transferring the undisputed portion of the amount payable by the Decca Fund, provided that the Decca Fund was placed at no risk. A loan was not legally possible but the Decca Fund would make payment to the LMS Fund of the minimum amount to which each transferring member was entitled as at 31 March 1997 plus a reasonable investment return since then as determined by the Decca Fund’s administrators in their discretion. Each transferring member would have to consent and the arrangement would be without prejudice to the adjudication and any other

proceedings. The basis on which the amounts to be transferred were to be calculated were set out.

Agreement was reached on the form of the required consent by the transferring members and the transfers in the aggregate amount of R1,794,082.00 duly took place from the Decca Fund to the Superflex Fund.

In a letter dated 13 September 1998, WWB requested further particulars to the complaint and informed ENF that the Decca Fund's actuary was investigating whether there still was

a surplus in the Decca Fund after the recent stock market crash as it would seem that the answer to this question might have a material effect on the proceedings before the Adjudicator.

In a letter dated 4 November 1998 the actuaries, Clemans, Murfin and Rolland, stated that the accrued actuarial reserve value on 1 April 1998 for the transferring members was R3,485,479.00 at that date. At 4 November 1998, the Decca Fund had a deficit of R175,000.00.

The complaint

The complaint, as is evident from the evidence, concerns the difference in opinion between the parties concerning the proper basis for the calculation of the amount transferable in respect of the complainants. The disagreement derives primarily from the different interpretations placed upon the relevant clauses of the sale and purchase agreement and the interpretation and application of the applicable legislation and rules. The enforcement of the agreement is most likely outside my jurisdiction. Nevertheless, it does have some evidentiary relevance. Moreover, the implementation of the agreement ultimately has led to the trustees of the respondent taking decisions which are the subject

of review and which form the basis of this complaint.

In general terms, the complaint relates to the administration of the fund, as well as the interpretation and application of its rules, and alleges a dispute of law relating to the fund's obligations in the current context and that the trustees have breached their fiduciary duties by improperly exercising their powers or by maladministering the fund resulting in prejudice to the complainants. As such the complaint falls within the definition of a complaint in section 1 of the Act.

From the documentation and written submissions it appears that no single decision of the trustees is the focus of review. Rather at issue is a series of decisions, or a course of events, culminating in a decision limiting the complainants' entitlement to their retrenchment benefits.

From the minutes of the meeting on 26 February 1998, it was clear that the majority of trustees, with section 14 of the Pension Funds Act in mind, resolved that the transfer of the actuarial reserves plus a share of the investment reserve would be reasonable and a sound basis to transfer assets to the new LMS fund. The trustees believed that a rule amendment would be necessary to achieve this objective, but subsequently failed to proceed with the amendment or its registration.

Subsequently, presumably acting on legal advice, the trustees have taken the view that no transfer of business was involved and that the complainants were only entitled to their retrenchment benefits. This position, is most evident in the correspondence addressed by WWB to ENF on 25 June 1998 and 8 September 1998. In the first letter the fund's legal representative comments as follows:

> Under the rules each member concerned was entitled to chose to take his or her benefit in cash or

to leave it in the fund or to transfer it to another fund. This option had to be exercised within 31 days after the benefit became due and payable, failing which the cash option would be deemed to have been selected. Our clients are however prepared to extend the period for exercise of the option so that the members concerned are not prejudiced.

Section 14 doe not in our view arise because there is no transfer by the fund of part or all of its business, i.e. assets and liabilities: benefits have become due and payable and the fund will simply pay them. The benefits may be transferred to another fund, subject to the members' rights under the rules, but it remains a payment of benefits and not a transfer of part of the fund's business as contemplated in section 14.

The second letter enlarges on the point, in the context of WWB proposing a solution on behalf of its client. The relevant part of this letter reads:

The trustees would however agree to an advance payment on the following basis:

1. The entitlements of the taken over members are governed in the first instance by the rules of the Decca fund. Under the rules as they presently stand:

   1.1_ each taken over member became entitled on ceasing to be employed by a participating employer to the early retirement/withdrawal benefits under the rules:

   1.2_ in the case of taken over members who qualified for a pension under rule 23.2.1 the members concerned would presumably wish, if their claims in the adjudication proceedings fail, to elect - in accordance with rule 26.1 - a deferred pension payable by the Decca fund rather than a cash transfer to the Litton fund equal to their retrenchment benefit in accordance with rule 24.2. There would therefore be no money available from this source for transfer to the Litton fund;

1.3_ in the case of early withdrawal our clients are willing to treat the early withdrawal as a retrenchment under rule 28.2. The members concerned had the option to take these benefits in cash or to transfer them to another fund or to leave them in the Decca fund as deferred pension benefits - rule 29.1. As they did not exercise this option with in 31 days they are now deemed to have exercised the option to take the benefits in cash - rule 29.1 - and the cash amount has become subject to the deduction of income tax by the Decca fund in such amount as the Receiver of Revenue may direct. Accordingly, insofar as the rules are concerned, the net amounts of the benefits after tax are available for transfer, provided that the members concerned request payment by way of transfer to the Litton fund. (Litton will also need to agree, and the amounts available for transfer may need to be further reduced for the reasons dealt with below). The tax deductible would need to be estimated, on a reasonably conservative basis, by the administrators of the Decca fund in their discretion. (It is not proposed to pay the tax now as the liability for tax will depend on the outcome of the adjudication proceedings).

2. The taken over members have framed their claims in the adjudication proceedings on a different basis. Their claims, as our clients understand them, are that the members concerned are to be transferred as a group to the Litton fund, that this brings section 14 into operation and that their reasonable benefit expectations include not only their past service actuarial reserves taking into account future salary increased but also a share of the surplus. The amount transferred would then presumably be allocated among the taken over members' fund credits in the ratio of the actuarial reserves held by the Decca fund in respect of the members concerned. Our clients dispute this approach but say that if the claim is upheld the only amount to be transferred is the actuarial reserves relating to the taken over members. A problem however arises because the Litton fund is not a mirror image of the Decca

> fund, but a defined contribution fund. The actuarial reserves held in respect of certain members would then be likely to be less than their retrenchment benefit. It follows that the amount the Decca fund can safely transfer to the Litton fund in respect of each taken over member is the lower of the after-tax retrenchment benefit of the member and the actuarial reserve held in respect of the member.

On this basis, the dispute, broadly speaking, is whether the complainants' entitlement is determined exclusively in terms of the existing rules of the respondent as a payment of benefits or whether the statutory prescriptions require their entitlements to be determined on a different basis.

Dr Douglas, on behalf of the respondents, in his submissions neatly categorised the dispute as being whether the transferring employees are entitled to:

i. the retrenchment benefits provided for in the rules; or
ii. their proportionate shares of the actuarial reserves; or
iii. such shares together with proportionate shares of the investment reserve; or
iv. such shares together with proportionate shares of the surplus including investment reserves.

There are also disputes regarding the date of which the benefits entitlements must be

calculated and regarding the investment return to be added to or subtracted from the benefit entitlements thereafter.

The purpose of section 14

The key question for determination accordingly is whether the scheme or arrangement between Racal and LMS, impacting on the pension rights of the complainants, constitutes

an amalgamation or transfer as contemplated by section 14 of the Pension Funds Act, 1956. If it does, the scheme will have to be reasonable and equitable and must accord full rights to the member's reasonable benefit expectations which arguably may include a share of the investment reserve. Section 14 reads as follows:

Amalgamations and transfers

(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 off any force or effect unless -

(a) the scheme fro 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 purposes 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 persons concerned in terms of the rules of a fund concerned; and

(ii) to any additional benefits the payment of which has become established practice,

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 a 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;

(d) the registrar has been furnished with such evidence as he may require that the provisions of the said scheme and the provisions, in so far as they are applicable, of the rules of every registered fund which is a party to the transaction, have been carried out or that adequate arrangements have been made to carry out such provisions at such times as may be required by the said scheme;

(e) the registrar has forwarded a certificate to the principal officer of every such fund to he effect that all the requirements of this subsection have been satisfied.

2. Whenever a scheme for any transaction referred to in subsection (1) has come into force in accordance with the provisions of this section , the relevant assets and liabilities of the bodies so amalgamated shall respectively vest in and become binding upon the resultant body, or as the case may be, the relevant assets and liabilities of the body transferring its assets and liabilities or any portion thereof shall respectively vest in and become binding upon the body to which they are to be transferred.

3. The officer in charge of a deeds registry in which is registered any deed or other document relating to any asset which is transferred in accordance with the provisions of subsection (2), shall upon production to him by the person concerned of such deed or other document and of the certificate referred to in paragraph (e) of subsection (1), without payment of transfer duty, stamp duty, registration fees or charges, make the endorsements upon such deed or document and the alterations in his registers that are necessary by reason of the amalgamation or transfer.

4. A transaction effected in terms of this section shall not deprive any creditor of a party thereto (other than in his capacity as a member or a shareholder of such party)

> of any right or remedy which he had immediately prior to that date against any party to the transaction or against any member or shareholder or officer of such party.

Generally, the intention of the legislator in enacting section 14 can be inferred from the

language of the statute which must be read in its context. The context ought not to be limited only to the words and general scheme of the statute, but in order to give proper effect to the purpose of the statute, it should include the factual position known to Parliament at the time of its enactment, the surrounding circumstances or historical setting, contemporary exposition and other statutes on the same subject.

The purposive method of interpretation has been readily embraced by judges in South Africa in a number of cases. Lord Denning, in the *Discipline of Law* 21 is one of many judges who has advocated a purposive of approach to interpretation. He refers to the practice of the European courts as follows:

> When they come upon a situation which is to their minds within the spirit - but not the letter - of the legislation, they solve the problem by looking at the design and purpose of the legislation - and the effect which it sought to achieve. They then interpret the legislation so as to produce the desired effect.

On this basis, he makes a call to common law judges in the following terms:

> Even in interpreting our own legislation, we should do well to put aside our traditional approach and adopt a more liberal attitude. We should adopt such construction as will “promote the general legislative purpose” underlying the provision.

In endeavouring to interpret section 14, therefore, the starting point should be to ascertain its overall purpose.

Section 14 forms part of a regulatory scheme aimed at protecting the investment of members of pension funds by affording the Registrar of Pensions, and the Financial Services Board, investigative powers to ensure that the impact of corporate restructuring arrangements on pension rights is reasonable and equitable from the point of view of the affected members and the funds involved. Such a policy recognises that pension rights amount to deferred pay, rather than gratuities bestowed within the benevolence of the employer, and that members are entitled to have their investment values preserved where their employment relationship is modified as a consequence of a corporate restructuring over which they have no control.

Pension benefits are part of the costs of employing labour, they are part of the remuneration which labour receives for services rendered. They form an integral part of the industrial relations bargain. Hence, it is inappropriate to view them as a form of employer benevolence. The Occupational Pensions Board of the United Kingdom in its report, *Greater Security for the Rights and Expectations for the Members of Occupational Pension Schemes,* Cmnd. 8649 (1982), para. 4.10, captures the sentiment as follows:

> In the days when pension schemes were looked upon as a form of employer benevolence, it may have been easier to equate the employer with a *paterfamilias* endowing his infant successors with an inheritance held in trust, but the notion now seems increasing incongruous. Under trust law the employer is considered to be the "settlor" who endows the trust from which the members or "beneficiaries" draw their pensions, overlooking the fact that the members, as well as the employer often contribute to the scheme and the employer's contributions can scarcely be considered as an act of unilateral benevolence.

Accepting that pensions are deferred pay leads one to view the rules of pension funds, and statutory provisions protecting benefits, as the means of implementing a remunerative promise. In the fulfilment of that promise the employer should act in good faith and the trustees of the pension fund are obliged to act with appropriate diligence and impartiality to ensure that the members' interests are protected and are suitably balanced against the employer's interests.

Section 14 of the Pension Fund Act is therefore a part of the broader legislative scheme to socialise legal relationships in the employment context. In relation to property and

contractual rights such legislation entails a shift away from an individualistic perception of rights towards the notion that property, in the sense of a power relation over the distribution and utilisation of resources, (including contractual obligations and entitlements), is a social responsibility. The institution of property in the broader sense is derived from and protected by society, i.e. it is a social institution and must be harnessed to serve particular social objectives. This is accomplished through the regulation of the use and application of resources in the form of protective legislation.

Section 14(1)(c), in particular, requiring as it does transfers to be reasonable and equitable, must be seen within the context of this general scheme of socialisation. As stated in *Lorentz v Tek Corporation Provident Fund and Others* 1998 (1) SA 192 (W), 229 pension funds should be construed contextually as being an integral part of the employer-employee relationship. Its provisions, therefore, ought to be construed holistically in conjunction with general legislative policy governing security on transfer of employment as currently reflected in section 197 of the Labour Relations Act, of 1996.

At common law where an employer sells its business, the purchaser is under no obligation to enter into contracts of employment with the employees of the seller. The transfer of contracts of employment was a matter for negotiation and agreement between the parties and the employees concerned. The Industrial Court under the unfair labour practice jurisdiction recognised the need to protect employees under these circumstances by requiring fair retrenchment procedures. In *Kebeni v Cementile Products (Ciskei) (Pty) Ltd* (1987) 8 *ILJ* 442 (IC) the court made reference to the British Transfer of Undertakings: Protection of Employment Regulations of 1981, which provide for the automatic transfer of contracts when a business is sold as a going concern and which were adopted in

accordance with European Community Law. However, the court hesitated to order a remedy along the lines of the regulations because this would have had major socio-economic policy implications.

Consequently, prior to the introduction of section 197 of the Labour Relations Act, employees had no right to continued employment on the transfer of the business where they worked. Section 197 now creates such a right and brings our law in line with the European provision. The effect of the provision is generally to ensure that an employee's continuity of employment is not interrupted by the transfer of the employer's business. A transfer of contract of employment takes place if the whole or any part of a business, trade or undertaking is transferred by the old employer as a going concern. In terms of section 197(2)(a) if an employer's business is transferred in solvent circumstances, unless otherwise agreed, all the rights and obligations between the old employer and the transferring employees at the time of the transfer continue in force as if they had been rights and obligations between the new employer and the transferring employees and the new employer is generally placed into the shoes of the old employer.

Section 197 of the Labour Relations Act does not automatically guarantee pension rights deriving from the relationship between the pension fund and the employee in his or her capacity as a member of the fund. The continuity of rights and obligations secured by section 197 is limited to those rights existing between the employer and the employee, which may include some but not all pension rights. The failure of section 197 to guarantee full continuity in pension rights (among the most significant of all employment rights) is explicable by the fact that the legislature presumably considered the matter adequately catered for by section 14 of the Pension Funds Act.

Section 14 is a generic provision governing all transactions involving the amalgamation and the transfer of pension fund business, regardless of whether such scheme or arrangement involves the transfer of contracts of employment. Thus, the provision is frequently applied to regulate transfers between pension funds when no transfer of

employment occurs and usually where the employer is a participating employer in both funds. Nevertheless, the provision unquestionably has application where contracts of employment are transferred in such a way requiring the employees to transfer from one pension fund to another. In which event, the protections afforded by section 14 of the Pension Funds Act supplement the protections provided by section 197 of the Labour Relations Act and should be construed in a similar vein to enhance continuity and the security afforded to employees to receive the maximum benefit of their deferred pay.

The protective scheme enacted by section 14 imposes a disclosure and reporting obligation on any fund involved in an amalgamation or transfer, and invests the Registrar, in his supervisory and regulatory capacity, with a significant authority to protect member rights and interests and to allow for equitable adjustment. In particular it requires that no amalgamation or transfers shall have any legal force or effect unless the Registrar is satisfied that the scheme effecting the proposed amalgamation or transfer :

i is reasonable and equitable;

ii accords full recognition to the rights of the persons concerned in terms of the rules of the fund;

iii accords full recognition to the reasonable benefit expectations of the persons concerned in terms of the rules of the fund;

iv accords full recognition to any additional benefits the payment of which has become an established practice; and

v would not render any fund which is a party to the scheme unable to meet the requirements of the Act or to remain in a sound financial position, if it is to continue after the implementation of the scheme.

Accordingly, the provision requires a full and proper investigation by the Registrar to determine the legality, reasonableness, equity, financial soundness and actuarial prudence of any such scheme.

The reporting and disclosure requirements of the provision are geared towards facilitating the investigation and determination by the Registrar. Section 14(1)(a) obliges the funds to submit every actuarial or other statement taken into account for the purposes of the scheme. Section 14(1)(b) and (d), as well as section 21, empower the Registrar to seek such additional particulars or evidence as he may require or deem necessary for the purpose of an investigation and the implementation of the scheme. On the basis of the documentation gathered the Registrar is then obliged to satisfy himself that the scheme meets the requirements of section 14(1)(c). The decision of the Registrar is reviewable before the ordinary courts or appealable before the appeal board established under section 26 of the Financial Services Board Act. As an administrative official he must exercise his discretion properly in accordance with the dictates of administrative law and the Constitution.

Other provisions of the Pension Funds Act strengthen the Registrar's supervisory and regulatory role in an amalgamation or transfer situation. Section 24 and 25 grant the Registrar general powers of investigation and inspection. In terms of section 26, if pursuant to his investigation the Registrar considers it necessary, he may apply to the High Court for an order directing that the rules regulating the management of the fund be altered in a specified manner. Likewise, in terms of section 27, the Registrar may apply to the court for the cancellation or suspension of the registration of the fund, if in his opinion, after his investigation, such a course of action is desirable or necessary.

Against this general background I now turn to the question of whether the scheme involving the complainants falls within the purview of section 14 and the regulatory powers of the Registrar.

Section 14 and the scheme under consideration

However before dealing with section 14, further thought needs to be given to categorising the termination of the complainants' membership in terms of the rules. Mr Jonker, on behalf of the complainants, submitted that the sale of the business of a division of Decca (SA) (Pty) Ltd to LMS on 27 February 1997 was structured, from a labour relations point of view, as a sale of a business as a going concern. Consequently, section 197 of the Labour Relations Act of 1995 governed the transfer of the contracts of employment. It was correctly conceded that section 197 only affects the rights and obligations between employer and employee and not between pension fund and member. However, he argued, pension fund trustees ought not to make decisions about the transfer of assets or termination of membership in the context of a sale of business without considering the reason for the departure of members from the fund. As I understand Mr Jonker's argument, the transfer or assignment of a contract of employment from one employer to another should be seen as a species of contractual termination different from a resignation or dismissal on the grounds of misconduct, incapacity or operational requirements. The Labour Relations Act clearly draws a distinction between a dismissal on operational requirements grounds (retrenchment) and transfers of employment. Likewise, section 14 of the Pension Funds Act contemplates this special category of termination of employment, which in this instance is not specifically provided for in the rules of the fund. Accordingly, the rights of the complainants should be determined primarily with reference to the Pension Funds Act and not solely in terms of the existing rules which do not provide for transactions as contemplated in section 14.

In arguing that the rules (in particular rule 28 dealing with the termination of employment) do not regulate transfers such as the one involving the complainants, Mr Jonker suggested that rule 35, dealing with take overs or amalgamations and entitling members to a share of the fund, could (by a process of extensive interpretation or analogy) be applicable to this situation. In this instance LMS purchased the assets and business of a division of Racal

SA, being a very small part of worldwide purchase by LMS from Racal. Take overs usually involve the assumption of control or ownership of a business concerned by another company by the acquisition of the majority of its shares, either by agreement or after a take over bid. Similarly, the blending of two concerns normally associated with an amalgamation, has not occurred in this instance. On these grounds, Mr Jonker conceded that rule 35 could have no direct application in the present circumstances. However, he argued that a sale of a part of a business of the participating employer was sufficiently analogous to a take over to allow for an application of rule 35, or at least the consideration of the rule as a guideline by the trustees, when exercising a discretion regarding the complainant's withdrawal rights. Such a discretion could be exercised in rule terms of rule 43 of the rules which provides as follows:

> On the occurrence of an event which has not been provided for in terms of the rules, the decision of the trustees in consultation with the employer, if not in consistent with the provisions of these rules shall be final and conclusive.

In sum, therefore, although the rules do not provide for the situation where the employer's business or part of the business is sold, it was submitted that the trustees in consultation with the participating employer, should have at least considered rule 35 as a guideline when exercising their discretion and ought not to limit themselves to considering the complainants' withdrawal as a termination of employment to be dealt in terms within the narrow confines of rule 28.

Dr Douglas, on behalf of the respondents, argued that the rule applicable in the present situation is indeed rule 28 (2) which provides that on retrenchment a member is entitled to twice his accumulated contributions, which are defined in rule 4 as the member's contributions to the fund plus an investment return factor. In his view, the sale of part of a business cannot be equated with the amalgamation or the take over of the employer as contemplated in rule 35.

For reasons which shall become apparent, I do not consider it necessary to pursue the

merits of the argument based on rule 35. It may indeed be an equitable consideration. But the principal issue, in my view, is whether or not the termination of the complainants' membership, and the transfer of their contracts under section 197 of the Labour Relations Act, can be considered to be a retrenchment and as such not qualifying as an amalgamation or a transfer of business within the meaning of section 14, and thus outside the supervisory net of the Registrar.

Rule 28(2) provides that if a member is retrenched by his employer and does not opt for early retirement he shall be entitled to a benefit equal to twice his accumulated contributions. Rule 29 grants the member the option to receive the retrenchment withdrawal benefit as a cash refund or to transfer it to an approved fund in terms of rule 24.2, or alternatively to preserve the benefit within the fund. Because rule 28 provides especially for retrenchment according to Dr Douglas it cannot be interpreted to give members the right to share in the surplus. The term retrenchment is not defined in the rules. Nevertheless, Dr Douglas contended that the ordinary, grammatical meaning of the term refers to the termination of an employee's employment because his services are no longer needed, usually due to the downsizing of the employer's business. The fact that the parties to the sale agreement decided to avail themselves of the statutory right under section 197 of the Labour Relations Act to transfer the employees without reference to them, and the fact that the statute accordingly afforded the employee certain protections arising out of the retrenchment by the old employer and transfer to the new employer, does not alter the nature of the termination of employment by the old employer, and the rules must be construed accordingly.

While there may be some merit in Dr Douglas' argument that a section 197 transfer of employment amounts to a retrenchment or a dismissal on operational requirement grounds, it need not follow that the rights of such employees are determined exclusively with reference to an antiquated and anachronistic pension fund rule regulating retrenchment. Such an argument, with respect, suggests an inability to get beyond the narrow contractual jurisprudence of yesteryear and a reluctance to acknowledge the law's

organic response to the status issues underlying the employment relationship.

Firstly, the Labour Relations Act, for evident policy reasons, draws a clear distinction between dismissals on operational requirement grounds leading to the termination of the employment contract and ultimately the employment relationship, on the one hand, (governed by section 189); and the transfer of a contract of employment resulting in the extinguishing of one party's obligations, but continuing an employment relationship with a substituted employer on similar contractual terms, on the other (governed by section 197). The idea of an employment relationship, superseding as it does the employment contract, has its origins in the statutory protection afforded by the unfair labour practice concept, now entrenched in section 23(1) of the Constitution. Where an employment relationship is expected to continue, the legislative scheme (as reflected in the Labour Relations Act, the Pension Funds Act and the Constitution) aims at protectively securing entitlements on reasonable and equitable terms. In *National Automobile and Allied Union v Borg-Warner SA (Pty) Ltd* (1994) 15 *ILJ* 509 (A), van den Heever JA pronounced on the concept of an employment relationship in the following terms:

> Under the common law, parties conclude a contract under which one of them is to provide services in return for payment. Their agreement determines when the relationship so constituted starts; what reciprocal rights and duties are required and incurred by each; and, if it is to be of indefinite duration, how it may be terminated.
>
> The unmistakable intent of labour legislation generally, is to intrude, or to permit the intrusion of third parties, on this relationship in innumerable ways. The intrusion as regards the content of the relationship is readily apparent in statutes such as the Basic Conditions of the Employment Act 3 of 1983 and the Wage Act 5 of 1957. The Act we are concerned with (the Labour Relations Act) - the primary purpose of which is to ensure industrial peace by the promotion of collective bargaining - does that, and more. It goes beyond intruding, or permitting intrusion by others, as regards the terms which govern the relationship while it lasts. It envisages intrusion as regards the very duration of the relationship, regardless of common law notions of consensus between the individual employer and employee on that score.

Secondly, and perhaps more importantly, the fact that the termination of the complainants' employment may fall within the concept of retrenchment regulated by rule 28, does not put an end to the matter. Such a classification in itself does not exclude the transaction from the purview of section 14 of the Pension Funds Act. The point in dispute is whether the transaction involves the transfer of any business from a registered fund to any other person in terms of section 14(1). If it is, the complainants acquire statutory rights regardless of how one may classify the termination of any contractual rights involved.

No matter how the rules or the parties view the matter, the issue must be determined objectively with reference to the purpose and intention of the legislature. The expression "transfer of business" is not defined in the Pension Funds Act. The term is wide enough to include every single exit and withdrawal of membership from a fund. The general policy and purpose of the provision favours some limitation recognising that the net of regulation is aimed at transactions having a potential to impact significantly on the financial soundness of the fund. Generally, one may safely assume, voluntary individual withdrawals fall outside the ambit of the provision. Clearer guidelines and criteria in the legislation would have been helpful. Nevertheless, a common sense approach supports a finding that the section is applicable when 60% of the membership of one fund moves to another, as in this case.

In Pension Fund Circular 78, issued by the Financial Services Board in February 1993, the Registrar offers some guidance: It provides:-

> No transaction involving the amalgamation or transfer of any business carried on by a registered fund with that of any other person is valid unless the provisions of section 14 have been complied with. The only transaction which does not fall within the ambit of section 14 of the Act is the voluntary transfer, by an individual member, of his benefit upon the cessation of his employment with his employer. Any other transaction constitutes the transfer of a business of a fund and therefore requires the Registrar's sanction in terms of section 14(1)(e) of the Act to be of force.

On this interpretation of section 14 and the concept of a transfer of business, the

arrangements relating to the complainants fall squarely within the ambit of section 14. My understanding is that there has been general compliance with the provisions of Circular 78.

The status of a pension fund circular as an aid to interpretation is open to debate. Prof Devenish, *Interpretation of Statutes,* 136, discusses the reliance on *subsecuta observatio* and *contemporanea expositio* as aids to interpretation and states:

> According to the literal theory, where the meaning of an Act is plain and unambiguous, it is not legitimate to resort to any such aid as afforded by usage, (*subsecuta observatio*) or contemporary exposition (*contemporanea expositio*). Where, however, a statute uses a word of doubtful meaning, the manner of acting under it for a long course of years sometimes gives an interpretation to the obscure meaning, and in such cases a construction which has long and publically been acted upon is not lightly disturbed.

Dr Douglas, on the other hand, relying on wording of section 14(2) argued that before a transfer can amount to a transfer of business in the meaning of section 14, there should be a transfer of assets and liabilities. The provision provides that once the scheme for a section 14(1) transaction comes into force the relevant assets and liabilities of the body transferring its assets and liabilities or any portion thereof shall vest in and become binding upon the body to which they are transferred. As the respondent is only transferring assets, or so the argument goes, there is no transfer of business.

I cannot agree with this interpretation. Firstly, while it is correct that the defined benefit liabilities existing in respect of the complainants prior to their transfer will not be transferred to the Superflex defined contribution fund, the Superflex on receipt of the assets will incur liabilities in accordance with the transfer agreement and in terms of its own rules. And to that extent liabilities can be said to have been transferred.

Even if I am mistaken in this interpretation, I remain unconvinced that a transfer of business necessarily involves a transfer of liabilities. Section 14(2) does not make it a

constitutive requirement of a transfer of business that liabilities should be transferred. It simply states that in the event of liabilities being transferred they shall become binding upon the body to which they are transferred once the scheme has come into force. Moreover, section 14(2) contemplates "any portion", of the assets and liabilities being transferred and a transfer solely of assets can constitute a transfer of a portion of assets and liabilities, if the expression is legitimately interpreted disjunctively. Furthermore, had the legislature intended to restrict the Registrar's supervision to those transactions involving transfers of assets and liabilities from a registered fund, one would have expected it to have used that expression rather than the more generic term "business". Section 14 is an interventionist, regulatory piece of legislation forming part of a broader scheme of consumer protection. A wide concept of transfer of business widens the net of consumer protection by ensuring that a broader spectrum of schemes impacting on investor rights are subject to the prudential regulation of the supervising authority. The overall aim is to ensure the soundness and efficiency of the system, and the protection of investors.

European Courts dealing with similar concepts in the employment context have given a generous and extensive interpretation to the concept of a transfer of business. Dr Stefan Lunk - *The New Labour Relations Act: Some remarks from the perspective of a German Labour Law Attorney,* (1997 *De Rebus*, 131) describes how the European courts have extended the concept in order to widen the regulatory net. He comments:

> At an early stage the courts held that apart from the "classical" transfer of assets such as large machinery, and depending on the kind of business involved, any takeover of assets would be sufficient as long as the purchaser acquired a functional organism enabling him to continue the business. For example, the Federal Labour Court of Germany has ruled that the purchase of customer lists which were the only asset of any substantial value in the seller's company constituted a transfer of business and thus led to a takeover of the company's staff. (BAG AP No 41 zu 613a BGB). The same was held regarding the transfer of a trademark which was the only asset of some value to the seller (BAG AP No 74 zu 613a BGB). The Federal Labour Court even ruled that the deliberate transfer of a specific employee who - due to his abilities and knowledge of customers -

> was of substantial value to the business could by itself constitute a transfer of business if the purchaser was thus in a position to continue the same business and had intended to do so. (BAG AP No104 zu 613a BGB).

While these comments are made in the specific context of transferring contracts of employment, the point remains that the expression "transfer of business" is open ended and should be interpreted to serve the broader regulatory purposes of section 14.

It will be recalled that clause 2 of part 2 of schedule 9 to the purchase and sale agreement governs transfers in respect of the pension entitlements of the complainants. Clause 2.2, in particular, provides that in respect of South Africa sufficient assets will be made available to fully cover liabilities accrued at the completion date, with allowance for future salary increases on the basis that this will be *transferred* to individual or collective pension arrangements for the transferring employees. Moreover, throughout much of the correspondence between the parties, the parties frequently refer to the pension arrangements as constituting a *transfer* and the entitlements of the complainants as *transfer values*. For example, Mr Hammond's letter of 12 March 1998, addressed to LMS, refers to the *basis of transfer* and *transfer payments*. This, of course, is not conclusive, but for what it is worth shows that the parties to the agreement saw the pension arrangements as constituting a transfer of business.

Accordingly, for the aforegoing reasons, I am satisfied that the transfer of the complainants out of the respondent as part of the purchase and sale transaction between LMS and Racal SA involves a transfer of business from a registered fund to another person and that the respondent is therefore obliged to comply with the provisions of section 14.

The board of management's statutory and fiduciary duties in a transfer situation.

Accepting that the transfer of the complainants falls within the net of section 14, the

trustees have certain statutory and fiduciary duties in that regard.

In terms of section 7C(1) the trustees are obliged to direct, control, and oversee the operations of the fund in accordance with the applicable laws and the rules of the fund. Moreover, section 7C(2)(a) requires the trustees in pursuing the objects of the fund to take all reasonable steps to ensure that the interests of members in terms of the rules of the fund and the provisions of the Pension Funds Act are protected at all times especially in the event of an amalgamation or transfer of any business contemplated in section 14. Further duties in section 7C(2) require the trustees to act with due care, diligence, good faith and with impartiality in respect of all members and beneficiaries.

These duties therefore compel the trustees when dealing the transfer of business to firstly follow the dictates of section 14. Section 7D(1)(f) requires the board to ensure that the rules and the operation and administration of the fund comply with the Pension Funds Act. This shall require the board to effect an appropriate amendment to the rules where the rules do not adequately cater for a transfer of business. The failure to effect an appropriate amendment conceivably will lead to a complaint of maladministration of the fund by any members sustaining prejudice.

Once the board is suitably empowered in terms of its rules to effect a transfer of business, the board is obliged to comply with the disclosure requirements of section 14 and, by implication, to ensure that the scheme is reasonable and equitable and accords full recognition to the rights and reasonable benefits expectations of the persons concerned in terms of the rules. The scheme must also accord full recognition to any additional benefits the payment of which has become established practice.

In passing, trustees should remember that Navsa J in the *Tek* case accepted counsel's argument that the reasonable benefit expectations of members cannot be restricted to the actuarial value of their interest in the fund, in accordance with the rules. If that were the case, it would have been unnecessary to amend section 14, as the Registrar always had

to be satisfied that both funds would, after the transfer, be in a sound financial condition. Accordingly, reasonable benefit expectations relate to expectations and benefits above and beyond the defined benefits. It is this interpretation which presumably is relied upon by transferring members to claim a right to share in the surplus of a fund, particularly the investment reserve.

The evidence shows that the trustees originally embarked upon this course of action. Correspondence from the principal officer of the fund indicates that it was the intention of the fund to make application in terms of section 14. At the meeting of 26 February 1998, the trustees agreed that the transfer of actuarial reserve including the investment reserve was a reasonable and sound basis to transfer the assets to the new fund. However, it will be recalled, at the behest of the employer and on receiving legal advice, the trustees retreated from this position on the understanding that the complainants were only entitled to their retrenchment benefit because they were advised that the transaction did not involve a transfer of business. Given the inherent ambiguity of the term, such legal advice cannot be considered unreasonable. To that extent, it mitigates the trustees' alleged breach of statutory duty in failing to comply with section 14. Be that as it may, the trustees remain obliged to follow the section 14 procedure.

Appropriate relief.

The complainants, on the assumption that I would find section 14 to be applicable, have advanced a detailed, complex and enlightening argument in support of the contention that I should prescribe to the trustees how to exercise their discretion concerning the transfer and the transfer values. The respondent has responded to the arguments in detail.

The argument proceeds on the assumption that the trustees of the fund were in breach of the statutory duties in section 7C and 7D and were in violation of the constitutional rights to just administrative action. With reference to various decisions of the trustees, the course of events and the circumstances surrounding the purchase and sale agreement, the

complainants submit that the failure of the trustees to exercise their duties of trust and care are so blatant that I have jurisdiction to set aside the decisions made by them and also to provide the trustees with clear and unequivocal directions on the exercise of their discretion in relation to the transferring employees.

As a remedy, the complainants request me to direct the trustees to transfer the complainants' actuarial value and investment reserve and a portion of the surplus, computed on the completion dated of 1 March 1997, and to direct the trustees to transfer the contributions accrued after the completion date, with actuarial interest of 12%. Considering that various methods might be applied for the computation of the actuarial reserve and the surplus, the complainant advances an appropriate test for testing the reasonableness and proportionality of the different methods of actuarial calculation and points to the share of the fund method as the best method not offending any of the fiduciary obligations of the trustees.

The argument assumes the trustees have reached a final decision on transfer values. The facts suggest otherwise. The original decision of the trustees taken on 26 February 1998 was superseded by the employer's intervention and the receipt of contrary legal advice. The subsequent events led the trustees to the conclusion that they were under no obligation to devise a reasonable and equitable scheme under section 14 and that the fund's obligation was no more than to pay retrenchment benefits. Even were I to accept this narrow and literalistic interpretation as amounting to chicanery or unreasonable prevarication, I doubt it would justify my substituting my decision for that of the trustees. The appropriate remedy in this instance is to remit the matter to the trustees to make a fresh decision. The determination of a reasonable and equitable transfer scheme according full recognition to the complainants' rights, benefit expectations and customary additional benefits involves a number of discretions and value judgments to be exercised and formed reasonably and in good faith by the trustees, subject to the prudential review of the Registrar. This involves a process of investigation and a proper balancing of competing interests on the basis of actuarial and financial advice. The process is

incomplete in this case, leaving me with inadequate information to substitute my decision for that of the trustees.

In short, the complainant is seeking to have me determine the reasonableness and equity of the scheme in advance of the trustees submitting the particulars of such a scheme to the Registrar. To this end arguments have been advanced concerning the legal and equitable entitlements of the various interested parties to share in the surplus and which deal also with the relevance of the source of the surplus.

Arguments about equitable entitlements to share in the surplus or the proportionality of various actuarial methods for determining transfer values cannot be evaluated and adjudicated upon in the abstract. Whether a particular distribution or method can be set aside as irrational, disproportionate or unreasonable will depend on the circumstances and the justification put forward by the trustees for the application of a chosen method. In this case the trustees have not applied themselves to the determination of reasonable and equitable transfer values. On the basis of legal advice they retreated to the position that no transfer of business was taking place and therefore that no reasonable and equitable transfer values had to be determined.

Accordingly, the arguments concerning the source and distribution of the surplus are premature.

The respondent, on the other hand, advances a rule-based argument to the effect that the trustees have no power in terms of the rules to grant the transferring employees anything other than their retrenchment benefits. Any appropriation of the surplus as part of an equitable scheme would be unlawful by virtue of the rules granting no such power. The argument is flawed for two reasons. Firstly, rule 44, in my view, gives the trustees the power to effect a transfer of business which is reasonable and equitable in accordance with section 14. The relevant rule reads:-

General Authority

Subject to the provisions of the Act, the Trustees shall be entitled in their absolute discretion to make arrangements and to do anything which is consistent with the provisions of these Rules or make any amendment which , in their opinion, is for the benefit and protection of members of other persons in receipt of or prospectively entitled to benefits under the fund.

Insofar as there may be any inconsistency between the requirements of a section 14 transfer and the rules regulating any increase in benefits, then by virtue of section 7D(1)(f) of the Pension Funds Act, the trustees are obliged to amend the rules to eliminate the inconsistency. Rule 37.1 grants the trustees the power to amend the rules or to alter or rescind any existing rules as they may deem fit. Dr Douglas' contrary submission notwithstanding, there is no requirement of employer consent to amend the rules to make such a decision.

Be that as it may, as stated, the relief sought by the complainants is inappropriate. Were I to identify the method for determining the complainant's actuarial values, and to allocate a portion of the surplus to the members, I would essentially be usurping the function of the trustees and the Registrar when I have neither the legal authority, nor the evidentiary basis to do so. As discussed, section 14 envisages a process of investigation and evaluation by the inspectorate and actuaries in the employ of the Financial Services Board. Decisions taken in that process are based on actuarial and financial data after it has been properly analysed and evaluated. The section 14 procedure entails a process of submission, negotiation, recommendation and ultimately decision by the Registrar. None of this has happened yet.

Moreover, were I to direct the transfer of actuarial reserve values, I have no means of knowing whether such values will be reasonable and equitable in respect of each complainant. Indeed, the transfer of an actuarial reserve value in respect of younger members may be unfair and could amount to less than the retrenchment benefit. No doubt there are other financial and actuarial considerations not apparent in the

documentation submitted in these proceedings which may have an impact on the equity of the scheme and which may only emerge in the process of the Registrar's investigations.

For these reasons, the appropriate relief is to direct the trustees of the respondent to submit the scheme for the proposed transaction to the Registrar for investigation and evaluation in terms of section 14.

Basis of continued contributions between 1 March 1997 and 31 March 1998

After the transfer of the complainant's contracts to LMS, contributions on their behalf continued to be paid to the respondent until 31 March 1998 on the basis that the transferring employees, despite the fact that they were probably ineligible in terms of the rules, remained as *de facto* members of the fund.

This irregular situation has created a conundrum in respect of the proper treatment of these amounts. The complainants submit that the payments were accepted as part of an interim arrangement pending initially the establishment of a new fund and from about middle 1997, the settlement of the dispute about the calculation of the transfer values. They submit that the trustees had a duty to act as common law trustees of assets held on behalf of the third party, in this case, the transferee fund. Hence, they seek an order directing the trustees to transfer these contributions with actuarial interest to the Superflex Fund.

The respondents contend that the contributions were paid on the basis that the transferring employees would remain members of the fund and that the rules would be amended retrospectively accordingly. They point to the fact that the transferring employees remained covered by the risk benefits and that benefits which became payable to transferring employees who ceased to be members during this period were calculated and paid out by the fund on the basis that they had remained members after 1 March 1997. Accordingly, in its view, the proper date for the calculation of the quantum of the

benefits payable in respect of the transferring employees is 31 March 1998 when at the insistence of Racal the complainants ceased to be members of the fund.

A further dispute concerns the fate of the complainants' investment in the fund after 31 March 1998. In response to the respondent's view that members who leave their assets in the fund should accept the assets to suffer the same fate as the other assets of the fund, the complainants submit that the transferring members can expect more from the trustees than this. In respect of assets identified as being in dispute, the transferring members, according to complainants, can reasonably expect the assets to be protected against market instability.

The respondent's response to this is twofold. Firstly, it argues that at no stage did the complainants or the new employer request that the transferrable amount be dis-invested from equity investments and transferred to another investment medium. Secondly, it contends that it was an implied term of the arrangements between the parties that the transferrable amount would remain invested as before until actual transfer and would accrue the actual rate of investment return by the fund, even after 31 March 1998.

I am in agreement with Dr Douglas that this difficulty amounts to a dispute of fact which can be resolved only after receiving the evidence of those involved in the arrangements concerning the continuation of contributions. It appears that the complainants' entitlement in respect of these amounts will be determined either in terms of the rules of the fund, with reference to any applicable contract, or in accordance with the principles of unjustified enrichment. The dispute will require resolution before the conclusion of the section 14 transfer. The Registrar shall have to make a finding on the matter in order to satisfy himself that the section 14(1)(a) scheme is reasonable and equitable and accords full recognition to the rights of the persons concerned. In addition, by receiving evidence on the matter the Registrar shall have a proper opportunity to satisfy himself as to compliance with the requirements of Circular PF 97 concerning the reasonableness and equity of the effective date of transfer and an appropriate rate of return from the effective date to the

date of payment, taking into account the fund's exposure to risk.

There will be no need to delay the section 14 process. The trustees can submit the scheme for the proposed transfer to the Registrar on the basis of their understanding of the rights concerning the contributions paid after 1 March 1997. The complainants likewise can make appropriate submissions to the Registrar.

I am aware that the complainants feel a sense of grievance and urgency in relation to the manner in which the trustees have dealt with their transfer. The dispute of law regrettably made the delays unavoidable. Nevertheless, the provisional transfer of monies by the respondent hopefully has eased the situation in the interim. The time limits contained in this order aim to expedite finality. I also shall request the Registrar to take reasonable steps to expedite the section 14 process, and if necessary to invoke the procedures in section 24 and 25. No doubt the Registrar shall take full cognizance of this determination.

The order of this tribunal is as follows:

1. The transaction involving the termination of the complainants' membership of the respondent is declared to be a "transfer of any business from a registered fund to any other person" within the meaning of section 14 of the Pension Funds Act, 1956.

2. The trustees of the respondent are directed to take all steps, including any necessary rule amendments, to comply fully with the provisions of section 14 and to transfer any business relating to the complainants pension entitlements to the Superflex Pension Fund within 6 weeks of the date of this determination.

DATED at CAPE TOWN this 5th day of MAY 1999.

_____

JOHN MURPHY

PENSION FUNDS ADJUDICATOR