IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO.:PFA/GA/486/99/AS

In the complaint between:

ALAN KENNETH SELF Complainant

and

NEDCOR PENSION FUND First Respondent

NEDCOR BANK LIMITED Second 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) of the Pension Funds Act of 1956.

The complainant is Alan Kenneth Self an erstwhile member of the first respondent and retired employee of the second respondent.

The first respondent is the Nedcor Pension Fund, a pension fund duly registered in terms of the Pension Funds Act of 1956. The second respondent is Nedcor Bank Limited a banking institution carrying on business as such and the former employer of the complainant.

The complaint relates to the administration of the fund and the investment of its funds and

alleges that the complainant has sustained prejudice in consequence of the maladministration of the fund. The complaint has two parts. The first relates to the failure of the first respondent to disinvest the complainant's transfer value from the fund on notification by the complainant that he wished this amount to be transferred to a preservation fund in accordance with a section 14 scheme, and the failure of the first respondent to invest such transfer value in a banking call account at an interest rate of approximately 16% from the time of notification to the time of transfer. The second complaint relates to the complainant's alleged rights to benefit from free Old Mutual shares which he contends ought to have benefited him and enhanced his asset value.

No hearing was held in this matter but a report was placed before me by investigator Antonia Simmons. Accordingly, in determining this matter I have relied on the documentation and report placed before me. Having completed my investigations I have determined this complaint as follows and for the reasons set out herein.

Background to Complaint

The complainant commenced employment with the second respondent on 1 May 1973 as Systems Analyst in the Computer Department, and retired on 31 August 1993 but continued to act as a consultant to the Information Technology Division until 30 June 1998.

Throughout his employment he was a member of the first respondent, a defined benefit fund, and made regular contributions towards his defined benefit.

At the date of retirement the complainant elected to become a deferred pensioner. It is common cause between the parties that the complainant was entitled to become a deferred pensioner and that the rules regarding his deferred pension were correctly applied to him at the time of his retirement.

In September 1997 the first respondent contacted the complainant in order to confirm his

personal details and correct address with a view to offering the complainant the opportunity to transfer his money to either a preservation fund or a retirement annuity.

In order to implement the necessary section 14 scheme and in accordance with a directive from this tribunal, it was necessary for the first respondent to effect a rule amendment. The relevant rules were rule 17bis, 24 and 25. The rule amendments were registered on 9 April 1998 by the Registrar of Pension Funds. In terms of the amendment the transfer value was to be the member's past service actuarial reserve in the fund as determined by the valuator together with such enhancements arising from any surplus in the fund as may be determined by the valuator as being in excess of funding requirements.

Towards the end of February 1998 the complainant received a letter from the first respondent addressed to all deferred pensioners of the first respondent. This letter contained the offer to transfer the benefit hitherto retained in the first respondent to either a preservation or a retirement annuity fund. Details regarding the possible transfers were explained in the letter as were the enhancements which would be applied. Pensioners were invited to seek assistance with further queries during office hours at various telephone numbers.

Important points in the letter of February 1998 which are of relevance to this determination are the following:

> Should you elect to transfer your money out of the Nedcor Pension Fund to a retirement vehicle of your choice, your transfer value will earn the yield in the Nedcor Pension Fund from 1 January 1998 to the date of actual transfer of your money to a retirement annuity or preservation fund of your choice.

and

> SPECIAL NOTE:

> Members are advised that transfer of the above money is subject to approval of the Section 14 certificates by the Registrar of Pension Funds as well as the registration of the amended Rules of the Nedcor Pension Fund.

As an annexure to his copy of the letter the complainant received a document entitled "Transfer Value Estimate" which supplied details of the estimated benefit available for transfer from the first respondent. This amount was stated to be R1 085 179.00. The complainant was also notified that he would receive a final Transfer Value Certificate as at 1 March 1998.

On 25 February 1998 the complainant completed an option form indicating that he wished to transfer his pension to a preservation fund. He requested his benefit to be transferred to the Protektor Preservation Fund underwritten by Old Mutual. On 20 March 1998 he also signed an indemnity form indemnifying the first respondent from and against any further claim upon its assets for retirement benefit.

The complainant's financial advisor was informed by the first respondent in a letter dated 31 July 1998 that the estimated value of the complainant's deferred pension as at 1 March 1998 was R1 094 000.00 but stipulated that the figure was for quotation purposes only and was subject to confirmation by the actuary. The financial advisor was requested to supply certain documentation from the transferee fund in order for the transfer to be effected.

Alexander Forbes was eventually in a position to apply to the Registrar for section 14 approval during September 1998, after receipt of the required information from the transferee fund, and submitted the application on 29 September 1998. The approval was received from the Registrar on 29 October 1998.

On 4 November 1998 an employee of the first respondent informed the complainant's financial adviser by telephone that the section 14 certificate had been finally approved and that they required the proposal number of the complainant's application to Old Mutual's Protektor Pension Fund and the banking details of the fund in order to effect the transfer

from the first respondent to the new fund. At this time the first respondent also stated that the amount which would be transferred would be the sum of R1 076 493.00. The transfer was effected on 18 December 1998 together with interest from 3 November 1998.

It is, further, relevant with regard to the second complaint that in terms of public announcements made by Old Mutual arising from Old Mutual's demutualisation stake holders who had invested in Old Mutual's products and were members of Old Mutual at midnight on 25 September 1998 would qualify for an allocation of free shares. Membership on the stipulated date entitled the member to certain numbers of free shares as determined by Old Mutual.

Complaint 1

The complainant noting that his transfer value was R1 076 493.00, some R17 507.00 less than the amount quoted on 1 March 1998, complained to the principal officer. He also complained about the failure of the first respondent to invest the transfer value in a suitable interest bearing account pending transfer. The first respondent had, in fact, invested the transfer value in a hedged portfolio in order to protect transferring members' interests. As a result, however, of a substantial drop in money markets even despite the hedge value was lost.

The complainant argues as follows:

1. In signing the option form for transfer of his funds he entered into a contractual relationship with the first respondent. He contends that the trustees of the first respondent were negligent for not disinvesting his investment out of the market at the time he accepted the offer pending the transfer to the Protektor Preservation Fund. He claims there was a duty upon the first respondent to ensure that his benefit not only retained its value but

appreciated in value.

2. The trustees were aware of the investment risk to which the assets would be exposed as they did implement a hedge cover up until 15 April 1998. He alleges that this cover expired on 15 April 1998 and that no precautions were taken after that date to protect the interests of deferred pensioners opting to transfer out of the fund. The trustees were clearly aware of the risks involved and nevertheless failed to guard against the possible harm.

3. There were excessive delays between his authorising the transfer of his benefits and the date of transfer. Had his application been processed within a reasonable time he would not have been prejudiced by the loss suffered by the fund as his portion of the fund assets would have been transferred to an Old Mutual Protektor fund policy and placed in a money market portfolio which would have yielded a growth of approximately 11.5% (16% per annum) between 1 March 1998 and 4 November 1998.

The respondents' response is that the fund was entitled to restrict the growth to the yield earned (positive or negative) by the first respondent from 1 January 1998 to the date of actual transfer, and the complainant accepted this when he signed the option form. It took reasonable steps to preserve the assets of the fund, and to hedge against the detrimental effect of the drop in the market value of such assets. The hedge was extended twice, to 30 September 1998 and again to 1 June 1999. It obtained the relevant section 14 certificate in respect of the transfer of the transfer value to the complainant's nominated preservation fund and transferred of the funds within a reasonable time. It acted responsibly, with due regard to the interest of the complainant and without negligence. The first respondent therefore submits that the complainant has no basis in fact or in law for claiming the interest which he has claimed.

Complaint 2

The second complaint relates to the complainant's right to benefit from the allocation of free shares by Old Mutual consequent upon its demutualisation. The complainant has requested me to order

the first respondent to grant him some benefit from the free shares which the fund will ultimately receive from Old Mutual.

There are two parts to the second complaint:

1. The complaint states that any approved fund which had investments with Old Mutual as at 25 September 1998 would be allocated free shares by Old Mutual. The value of these free shares would ultimately benefit the members of the fund. Since his investment amount had not been transferred to Old Mutual Protektor Fund as at 25 September 1998 he would not receive any benefit of free shares from the Protektor Fund. He had thus suffered a loss as a result of the delay in transfer.

2. The complainant submits, that he should be entitled to benefit from any free shares which might be allocated to the first respondent. He contends that his financial advisor was given assurance by an employee of the first respondent that he would be a direct beneficiary of the demutualisation process of Old Mutual because his investment was still with the first respondent on 25 September 1998 and more specifically since this fund was invested with Old Mutual.

The complainant submits that any benefit earned by first respondent while he was a member of such fund must accrue to him by right on a pro rata basis and so too should the demutualisation benefits which are simply another form of accrual to which he has rights and which should not be treated differently from dividends, interest and capital growth. To suggest that first respondent has discretionary powers as to when and how to distribute such monies implies that the fund still has control of the funds of the withdrawing members and, negates the very reason why a member may have elected to leave the fund in the first instance.

The respondents reply to this complaint as follows:

1. In terms of the public announcement made by Old Mutual in regard to the entitlement to

free shares upon demutualisation only stake holders who invested in Old Mutual's products and were members of Old Mutual at midnight on 25 September 1998 qualified for an allocation of 200 free shares. Since the complainant's transfer value had not been transferred to the complainant's chosen preservation vehicle on 25 September 1998 he is consequently not entitled to an allocation of free shares on the basis of such investment. The delays in the transfer were moreover not unreasonable. The terms of the issue of the demutualisation shares further provide that, in addition to the 200 free shares to which a member is entitled if he was a member on 25 September 1998, he may be entitled to additional shares in respect of all policies held by him based on their value on 31 December 1997 . Complainant would therefore not have been entitled to such shares.

2. Notwithstanding the alleged assurance given by a staff member of the first respondent that the complainant would benefit directly from the demutualisation process because his investment was still with the first respondent on 25 September 1998, this is incorrect as the underlying assets of the fund of which the complainant's transfer value formed a part were, on 25 September 1998, not invested in Old Mutual but in a hedged portfolio. No free demutualisation shares accrued to the fund in respect of such hedged portfolio. There is no obligation to undertake that the complainant will receive some benefit from free shares ultimately received by the first respondent from Old Mutual or that complainant is entitled to any such benefit as of right. Should it at some time in the future, and after the fund had received any benefit of free shares consequent of the demutualisation of Old Mutual, be decided to allocate such benefit to members and/or former members of the fund, the complainant would be treated no differently from other former members in the same position. However, no such decision has been taken and that the first respondent is not obliged to take such decision until it is reasonably appraised of all the facts and implications of such benefit for all stakeholders.

The respondent therefore contends that this complainant too, should be dismissed.

Determination

Section 14 forms part of a regulatory scheme aimed at protecting the investment of members of pension funds by affording the Registrar of Pension Funds and the FSB, investigative powers to ensure that the impact of corporate restructuring arrangements on pension rights is reasonable and equitable from the point of view of affected members and the funds involved. If a transfer as contemplated by section 14 of the Pension Funds Act is effected the scheme would, therefore, have to be reasonable and equitable and should accord full rights to the member's reasonable benefit expectations.

The principle that the common law fiduciary duties apply to trustees of a pension fund is well established. Such duties are codified in sections 7C and D of the Pension Funds Act specifically in this instance, cognisance should be taken of the provisions of section 7C which makes specific reference to amalgamation or transfer of any business as contemplated in section 14. There is therefore a statutory obligation to ensure that interests of members are protected at all times and especially in the event of a transfer of business as contemplated in section 14, and for the board to act with due care, diligence and good faith, to avoid conflicts of interest and to act with impartiality in respect of all members and beneficiaries.

The enquiry in this complaint, therefore, is in essence whether the fiduciary duties have been complied with and whether the interests of the complainant have been adequately protected.

Regarding the first complaint in which the complainant seeks to obtain payment of compound interest at 16% on the benefits due to him, it is necessary, therefore, to consider whether the steps taken by the first respondent between the 25 February 1998 and the end of November 1998 in any way fall short of the standard of care, diligence and good faith required of them and whether reasonable steps were taken to protect the complainant's interests. The terms of transfer were agreed between the parties and are reflected in the letter of February 1998 cited above. In entering into a contractual relationship the parameters of the parties duties and obligations were established and agreed upon. The fact that certain contractual terms existed between the parties, however, will not of itself exonerate the first respondent from complying with its fiduciary duties. Provided the

contractual terms do not directly conflict with the fiduciary duties, the parties can reasonably be held to such contractual terms. It is in the nature of the investment of financial assets that it is always easier to determine the best means of investment *ex post facto*. The fiduciary duties of the first respondent cannot be expected to incorporate the wisdom of hindsight. The essential term governing transfer was that the transfer value would bear the fate of the fund pending transfer.

A common method utilised to preserve the assets of a fund from negative yield is by applying a policy of hedging. In this instance such hedging exercise was undertaken by the first respondent on the advice of financial experts and with the intention of protecting the interest of the deferred pensioners opting to transfer out of the fund. As a direct result of the hedging the negative yield on the transfer value during the appropriate time was only 1.63% at a time when the all share index on the Johannesburg Stock Exchange dropped by more than 18% and at a time when there were negative effects of the worldwide stock market corrections. The original hedging transaction which expired on 15 April 1998 was in fact extended as indicated by the first respondent. The hedging transactions were implemented in order to attempt to ensure that the member's interests were adequately protected and secured at a time of economic downturn. I find, therefore, that the first respondent complied with its fiduciary duties insofar as it took reasonable and adequate steps to protect the interests of the relevant members through its hedging exercise.

The terms of the contract which the complainant entered into were clearly stated in the letter directed to the complainant dated February 1998 and in response to which the complainant made his election. The complainant was, therefore, aware of the terms of the contract prior to his entering into the contract. The complainant does not appear to have raised concerns with the fact that he would be subject to the fund yield between 1 January 1998 and the final transfer of his funds at the time of entering into the contract. The complainant in fact did not raise the issue until such time as final transfer was made to the investment vehicle of his choice; nor did he make his acceptance of the contract conditional. I cannot find that the terms of the contract are *contra bonos mores* nor does the imposition of the terms of the contract in any way detract from the fiduciary duties of the trustees or the standard which should be imposed upon the trustees in relation to the assets of the members of the fund. In fact, PF Circular No. 97 inserts two additional questions in

the forms to be submitted when applying for a section 14 certificate. These require the transferor fund to state how the assets to be transferred will be adjusted for investment return earned across the period from the effective date to the date of payment, and where a rate other than the fund rate of return is to be used, to state what action the fund has taken to protect itself against a fall in the value of the assets across the period. The circular also states that:

> The default should be the investment return owned by the transferor fund, positive or negative, i.e. "fund rate of return".

The purpose of this new requirement is to ensure that the reasonable benefit expectations of both transferring members and those remaining in the fund are protected.

The remaining issue is to whether the respondent caused undue delay and acted without due diligence. All surrounding factors must be taken into account in order to determine the reasonableness of the respondent's conduct and the application of due diligence. In view of the magnitude of the exercise undertaken and the number of transfers involved I am unable to establish from the evidence before me that the first respondent was culpably dilatory in finalising the transfer. It would appear that documentation was required not only from the first respondent, but also from the new fund and it would be unreasonable to have expected the first respondent to pursue the progress made with documentation due by another fund more speedily than it did. I am satisfied, therefore, that while there were delays in making the final transfer, these delays were not excessive or unreasonable nor were they due solely to omissions on the part of the first respondent. It is not uncommon for the formalities required for transfer of funds to extend over a period of up to a year and even beyond. Time scales of eight or nine months are, unfortunately, not uncommon.

Accordingly the first complaint is dismissed.

Regarding the second complaint, the complainant is not entitled as of right to the benefits which may accrue to the defined benefit fund as a result of free shares granted to it. He is entitled to his defined benefits in terms of the rules, including an enhancement on transfer.

Any free shares issued to the fund on demutualisation belong to the fund and are to be applied reasonably by the board of management as it considers necessary to meet its ongoing liabilities and obligations.

The first respondent has indicated that in the event that it, at some future time and after it has received the benefit of free shares, decides upon the allocation of such benefit to members and/or former members of this fund, the complainant would be treated no differently from other former members in the same position. I am satisfied that in the event of such benefit being distributed amongst members or enhancing members or former member benefits the complainant would be taken account of. The fiduciary duties would at that time compel the trustees to make just and equitable decisions relating to such distributions. It would at this stage be imprudent to dictate to the trustees whether such benefit shall be distributed and/or when it shall be distributed and/or the manner of distribution. This is a matter which will be taken account of in the future at which time the complainant would be in a position to complain should he be treated differently from any other member of the fund.

Regarding the complainant's concern that he will not receive shares which will be allocated to members of the Old Mutual Protektor Fund as a result of the delay in the transfer of his value to Old Mutual, it has been confirmed, after discussion with Mr Chris Newall of Old Mutual, that in order to benefit from demutualisation it is necessary to have been a policy holder as at 31 December 1997. The complainant, in this instance, was not yet a member of the Old Mutual Protektor Fund at the relevant date and could not have been pursuant to the transfer from the first respondent. He, therefore, does not qualify to benefit from any allocation of free shares. In any event, the Old Mutual Protektor Fund is the policy holder and free shares will be allocated to the fund and not to individual members. Members could only benefit as decided by the trustees.

Accordingly, the second complaint is dismissed.

DATED at CAPE TOWN this 2nd day of July 1999.

John Murphy
Pension Funds Adjudicator