IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO: PFA/WE/15/98/JM

In the complaint between:

HC Barnard & Others **Complainant**

and

Langeberg Foods Pension Fund **Respondent**

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

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1. The complainants have lodged two separate complaints in terms of section 30A of the Pension Funds Act of 1956. In broad terms, the complaints relate to the restructuring of the pension fund and the complainants' rights as former members to share in the surplus assets of the fund.

2. On 12 December 2000, an attempt was made to settle the dispute by means of a mediation hearing in Cape Town. When the mediation exercise failed, a further hearing was held in Cape Town on 26 February 2001. The complainants were represented by D R Mitchell of Kritzinger & Co attorneys. The respondents were represented by Adv C Loxton SC and Adv A Franklin SC, instructed by C Evison of Deneys Reitz attorneys, Cape Town.

3. The first complaint was lodged on 29 July 1998. The second complaint was lodged in late January 2001 subsequent to the failure of the mediation process. I shall refer to the complaints respectively as the first and second complaint.

4. The forty-five complainants are all persons who since 31 July 1995 were either

retrenched or resigned from service with Langeberg Foods Limited ("the employer"). The services of all except nine of the complainants were terminated during the course of 1995. The others terminated their services during the course of 1996 or in early 1997.

5. Upon their departure from the fund all the complainants were paid the benefits owing to them in terms of the rules of the fund in the amount of his/her actuarial reserve. Most received cash payments, while ten of them transferred their benefits to preservation funds.

6. Shortly after the complainants' withdrawal, the fund commenced a process of restructuring which involved the creation of a defined benefit section in the fund for in-service members and the outsourcing of the pensioners to annuities with Sanlam Limited. Active members who elected to join the defined contribution section of the fund received a transfer value of their actuarial reserve values plus a 40% enhancement. The enhancement represented compensation for the transfer of the investment risk from the fund to the active members. Current pensioners, as I have intimated, were granted the option of purchasing annuities in their own names with effect from 1 October 1997. They received an additional pro rata 10% enhancement in their benefits and an annual 13th cheque to compensate for the transfer of the pension liability from the fund to Sanlam, and for their loss of entitlement to an employer subsidy in respect of post retirement medical aid benefits. The handful of existing members and pensioners of the fund who elected to remain in the defined benefit section of the fund received no enhancement to their benefit. Full details of the restructuring scheme and arrangements are set out in *Adriaens & others v Langeberg Food Pension Fund* [2000] 1 BPLR 1 (PFA).

7. The first complaint is in essence that the board of management of the fund ought to have included within the category of persons entitled to an enhancement all former members of the fund, including the complainants. They maintain that in the process of restructuring the fund, the board, in the proper exercise of its fiduciary duties to

members and former members, should have considered a more equitable distribution of the surplus which should have included an enhancement of the amounts paid to or transferred on behalf of the complainants. It is alleged that the board failed to evaluate the situation properly in that only in-service members and pensioners were given the benefit of a surplus distribution from assets built up on the investments of a broader category of members.

8. The complainants claim that as a result of their recent retrenchments they occupy a unique position, implicitly recognized by the fund's rules dealing with dissolution, resulting in their having retained a beneficial interest in the surplus assets of the fund. They consequently seek an order interdicting the fund from proceeding any further with the implementation of the restructuring and the payment of a fair and equitable enhancement of the actuarial reserve values paid out to each of them at the time of their retrenchment or resignation in the period between 1995 and 1997.

9. The complainants initially also argued that the employer as a rule should not be permitted to benefit from any surplus derived from a source other than itself. The proposition was based on the High Court's finding to that effect in *Tek Corporation Provident Fund & Others v Lorentz* [1999] (4) SA 884 (SCA), which was later overruled on appeal. However, in response to the decision on appeal, and subsequent to the failed mediation exercise, the complainants submitted a second complaint challenging the employer's entitlement to the surplus left over after the restructuring. In terms of rule 10 of the rules of the fund prior to the 1997 restructuring, the participating employers were constrained to make contributions to the fund as determined by the actuary as adequate to provide the benefits in terms of the rules. Participating employers were not entitled to reduce contributions at will, and any actuarial surplus was effectively subject to the recommendations of the board of management and the control of the actuary. Rule 12.4 was introduced into the rules with effect from 13 July 1998 as part of the defined contribution structure. In terms of rule 12.4(1)(a), the remaining actuarial surplus in the defined benefit section of the fund (after the transfers and outsourcing) was credited to a reserve account in the defined

contribution section. Rule 4.2 governing the employer's contributions, read with rule 12.4(2)(c) providing for debits to the reserve account, permits the employer after consultation with the board of management to direct the board to apply part of the surplus in the reserve account for the purpose of meeting its contributions to the fund. This would be possible even where the board of management and the actuary were opposed to such an arrangement. The employer is given a discretion to utilize the surplus for its own benefit to the prejudice of the members and former members. Thus, it is contended, the new rules are arbitrary since they permit the employer unrestricted access to the surplus, whereas previously this was subject to the reasonable control of the board and the actuary. The complainants, therefore, submit that the decisions adopting the rules constituting and governing the reserve account were in excess of the board's powers and amounted to maladministration prejudicial to the complainants. They seek an order striking down the rules for authorizing the arbitrary deprivation of property contrary to section 25(1) of the Constitution and also because (contrary to section 33(1) of the Constitution) they amount to administrative action which is unreasonable.

10. The fund has responded to the merits of both complaints and has raised certain points *in limine*. Because of the view I take in relation to the merits, it is unnecessary to deal with the points *in limine*.

11. The fund maintains that upon withdrawal, for reasons of redundancy or resignation, each complainant received the benefits due to him/her in terms of the rules. At the time the fund was restructured, the complainants had no rights in relation to the fund and could not have entertained any legitimate expectations which were impaired or infringed thereby. It is further contended that the board was under no duty, either in terms of the Act or the rules, to consider making or actually to make an enhancement to the benefits of former members who had withdrawn from the fund and who had received all benefits owing to them in terms of the rules.

12. The complaint raises squarely the question of the extent to which former members of

pension funds are entitled to share in the appropriation and distribution of surplus assets. Members of pension funds are as a rule entitled to the benefits provided for in the rules and once such have been paid they have no further claim against the fund. See *Horlock v Illovo Sugar Pension Fund and Another* [2000] 9 BPLR 997 (PFA); and *Kerr-Philips v Premier Retirement Fund* [2000] 10 BPLR 1106 (PFA). Unless special or exceptional circumstances exist, the board of a fund normally owes no fiduciary or contractual duty to former members who have been paid their benefits, except perhaps to consider their claims in good faith.

13. *Euijen v Nedcor Pension Fund* [2000] 5 BPLR 465 (PFA) is a matter in which we recognized some claim on the part of former members. The fund in that matter retrospectively enhanced the transfer values of certain former members still in the employ of the participating employer who had transferred out of the fund to a defined contribution fund established by the employer. The retrospective enhancement effectively amounted to a change in the transfer basis of the earlier transfers. The fund justified the enhancement on the grounds that at the time the former members transferred it was of the mistaken opinion that the surplus belonged exclusively to the employer. The issue for decision was whether the law or the rules of the fund prohibited the retrospective enhancement. With reference to the rules of the particular fund, I held that the distribution of part of the surplus (by means of a rule amendment) to former members of the fund, who still were employees of the employer, was consistent with the expressed objects of the fund to provide benefits to the employees of the employer. The objects were not restricted to providing benefits exclusively to members of the fund. The decision to treat the former members equitably could not be regarded as *mala fides,* nor did it amount to maladministration. The former members who had transferred on the basis of a mistaken supposition concerning the employer's entitlement to the surplus had a legitimate expectation in the circumstances to share in the surplus, especially in an ongoing restructuring of the pension arrangements of the employees of a single employer. I concluded with the following *obiter*:

Recognition of the legitimate expectations of former members of a pension fund to participate in the

> surplus is plainly the most just and equitable manner in dealing with its distribution, especially considering that such former members, through the investment of their contributions, may well have contributed substantially to the emergence of the surplus. To accept the complainant's argument that only the members of a fund are entitled to share in the surplus, may lead to the undesirable practice of leaving a minority of members as the only persons with rights and expectations to share in the surplus when a fund is wound up shortly after a retrenchment exercise. The practice is not unknown in South Africa. By according legitimate expectations to share in the surplus to former members, it is hoped that such practices will be reconsidered. The nature, content and the extent of the legitimate expectations of former members will vary according to the circumstances and will have to be determined on a case by case basis in the future.

14. It does not follow that former members who have received all of their benefits and who are no longer in the employ of the employer automatically have any rights or expectations to share in the assets of the fund. The restructuring arrangements in the *Euijen* matter were part of an ongoing scheme and the finding was limited to the conclusion that the trustees had not exceeded their powers. Moreover, the *Euijen* decision was handed down prior to the decision of the Supreme Court of Appeal in the *Tek* matter, and to the extent that the impression has been created that all former members have significant rights to share in the surplus, this must be seen as qualified by the pronouncement of the Supreme Court of Appeal that entitlements are determined primarily, if not exclusively, by the rules.

15. In terms of the Pension Funds Act, all the assets, rights, liabilities and obligations pertaining to the business of a pension fund are deemed to be assets, rights, liabilities and obligations of the fund to the exclusion of any other person, and no person has any claim on the assets except insofar as the claim has arisen in terms of the rules or has been incurred in connection with transactions relating to the business of the fund. Sections 12 and 13 of the Act give the rules statutory force, and section 7C provides that the objects of a board should be to direct control and oversee the operations of a fund in accordance with the applicable laws and the rules of the fund. Section 13 limits the claims of members and former members to entitlements in terms of the rules. It reads:

> Subject to the provisions of this Act, the rules of a registered fund shall be binding on the fund and the members, shareholders and officers thereof, and on any person who claims under the rules or whose claim is derived from a person so claiming.

16. Accordingly, the difficulty faced by the complainants is that they are no longer members of the fund. A member is defined in section 1 of the Act specifically to exclude a member or former member of the fund who has received all the benefits which may be due to him from the fund and membership has thereafter been terminated in accordance with the rules of the fund. Former members who have received all benefits due to them in terms of the rules and whose membership of the fund has been terminated are therefore not members as defined in the Act, and by virtue of section 13 have no claim against the fund.

17. In an attempt to overcome this, Mr Mitchell focused his attack on the restructuring decision and relied essentially on two propositions. Firstly, he asserted that the spirit of rule 29 providing for former members to share in the assets of the fund on liquidation should be applied to the restructuring arrangements. Since rule 29 makes provision for a limited category of former members to participate in the distribution of surplus on liquidation, and considering that a restructuring process is analogous to a liquidation, it was submitted that former members should have been allowed to participate in any benefit enhancements consequent upon the restructuring. From this it was further argued that the complainants retained a beneficial interest in the fund and its assets and that the concepts of good faith, reasonableness and equity support such a conclusion. I agree with Mr Loxton that this argument is problematic for the following reasons:

- The Adjudicator is bound to apply the law. As such, I have no equitable jurisdiction – see *Shell & BP South African Petrolium Refineries (Pty) Ltd v Murphy & Others* [2000] BPLR 953 (D) @ 958 E. The primary enquiry is to decide whether or not the rules of the fund have been properly applied in the circumstances of any case.

- Rule 29 does not apply in the present circumstances as there was no dissolution of the fund. A rule which is clear in its terms cannot be applied when a different but analogous situation arises. A similar argument advanced in *Tek* was dismissed by Marais J (at paragraph 28) in the following terms:

> An unavoidable consequence of the absence of appropriate provisions was that counsel for Respondent were constrained to rest their argument upon what they described as analogous provisions in the rules which, so it was said, gave "an indication" as to what should be done in this admittedly different situation. In my opinion there are serious conceptual difficulties in the way of such an approach. What the trustees may do with the fund's assets is set forth in the rules. If what they propose to do (or have been ordered to do) is not within the powers conferred upon them by the rules, they may not do it. They have no inherent and unlimited power as trustees to deal with a surplus as they see fit, notwithstanding their fiduciary duty to act in the best interests of the members and beneficiaries of the fund. It may seem odd to speak of powers being beyond the reach of the trustees and the employer when the rules empower them to amend the rules but the contradiction is more apparent than real. First, their substantive powers at any given moment are circumscribed by the rules as they are at that moment. The fact that power to change the rules exists is irrelevant when assessing whether or not the particular exercise of powers in question was *intra* or *ultra vires*. Secondly, there are a number of qualifications in both the rules and the Pension Funds Act to the exercise of the rule amending power conferred by rule 21. It is unnecessary to spell them out; it is sufficient to say that the trustees and the employer do not enjoy absolute autonomy in that regard.

- Finally, even were one justified in measuring the reasonableness of the board's decision against the spirit of rule 29, the only members who would benefit in terms of its provisions would be those who were members of the fund "immediately preceding the date of dissolution", and the complainants fall outside that category.

18. In a further attempt to overcome the difficulty, Mr Mitchell argued that on a proper construction of section 14 of the Pension Funds Act, it was incumbent upon the fund at the time of the complainants' withdrawal from the fund to have lodged a scheme with

the Registrar in terms of section 14 of the Act in respect of each of the complainants or at least those who had been retrenched. The termination of the complainants' membership, it was argued, amounted to transfers of business within the meaning of section 14 and it was thus necessary for the fund to have complied with its provisions. Because no scheme was lodged in terms of section 14 it resulted in the complainants remaining members of the fund. Accordingly, as members, the complainants enjoyed a contingent interest in the assets of the fund in consequence of their right to share in any distribution of surplus assets upon dissolution of the fund and they hence also had standing to challenge the decisions of the fund. Section 14(1) reads as follows:

> (1) No transaction involving the amalgamation of any business carried on by a registered fund with any business carried on by any other person (irrespective of whether that other person is or is not a registered fund), or the transfer of any business from a registered fund to any other person, or the transfer of any business from any other person to a registered fund shall be of any force or effect unless
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> (a) the scheme for the proposed transaction, including a copy of every actuarial or other statement taken into account for the purposes of the scheme, has been submitted to the registrar;
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> (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;
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> (c) the registrar is satisfied that the scheme referred to in paragraph (a) is reasonable and equitable and accords full recognition
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> (i) to the rights and reasonable benefit expectations of the persons concerned in terms of the rules of a fund concerned; and
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> (ii) to any additional benefits the payment of which has become established practice,
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> 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 the effect that all the requirements of this subsection have been satisfied.

19. Section 14(1) requires that schemes involving transfers of business be submitted to the Registrar. In this instance there was no amalgamation of business, but certification would be required were the withdrawals of the complainants to be considered to be transfers of "any business from a registered fund to any other person". The term "business" is not defined in the Act but would seem to mean any business carried on by a fund. The definition of a pension fund organization in section of the Act gives an indication of what is meant by business. The definition reads:

(a) any association of persons established with the object of providing annuities or lump sum payments for members or former members of such association upon their reaching retirement dates, or for the dependants of such members or former members upon the death of such members or former members; or

(b) any business carried on under a scheme or arrangement established with the object of providing annuities or lump sum payments for persons who belong or belonged to the class of persons for whose benefit that scheme or arrangement has been established, when they reach their retirement dates or for dependants of such persons upon the death of those persons,

and includes any such association or business which in addition to carrying on business in connection with any of the objects specified in paragraph (a) or (b) also carries on business in connection with any of the objects for which a friendly society may be established, as specified in section 2 of the Friendly Societies Act, 1956, or which is or may become liable for the payment of

> any benefits provided for in its rules, whether or not it continues to admit, or to collect contributions from or on behalf of, members;

20. Only a body which carries on the business of a pension fund can be described as a pension fund organization and it seems reasonable to conclude that such a body is the only person contemplated in section 14 as the possible recipient of pension fund business. Section 14 thus regulates transfers of business between pension funds. It is inconceivable that pension fund business should be transferred to bodies which are not pension funds as this could offer an expedient means of avoiding ongoing regulation. The transactions sought to be regulated are those in which the Registrar has an abiding obligation to provide prudential regulation and protection in the continuation of any pension fund business. Where the liability of a pension fund is extinguished by the payment of a benefit, there is no transfer of business requiring continuing supervision. The mere payment of benefits to members on retrenchment or resignation therefore cannot be construed as a transfer of business within the meaning of section 14.

21. Insofar as some complainants transferred to preservation funds, it is correct that a section 14 scheme should have been submitted to the Registrar in respect of their transfers. However, it does not follow that the failure to do so resulted in such complainants retaining their membership of the fund. The complainants who transferred to preservation funds still exited the fund and relinquished their membership by virtue of the termination of their employment and the receipt of the benefit which was due to them in terms of the rules. The fact that the contractual transfer of business between the two funds was void or voidable as between them does not mean that membership is automatically restored.

22. Mr Mitchell has also relied on what he describes as “the broad concepts of trust (good faith, reasonableness and equity) on which the concept of a pension fund is founded” to argue that the complainants retained a beneficial interest in the fund and its assets. Reasonableness and equity, he submitted, demand that surpluses should not be used

simply as a windfall for current members and that the interests of former members who left the fund within a reasonable period before the restructuring should be taken into account. These principles, he claimed, are derived from the general principles of the law of trust which are founded in equity and form part of South Africa's common law.

23. Such arguments are a brave attempt to enlarge the scope of former member entitlement. While one naturally has some sympathy for arguments founded in equity, there is no basis in law for this tribunal to assume an equitable jurisdiction of the kind suggested. First of all, pension funds are not trusts in our law. Trusts are not possessed of legal personality, whereas a pension fund is a corporate person at both common law and in terms of the Act. Moreover, trustees are determined by the deed of trust. There is no election or nomination as provided for in the Pension Funds Act. Likewise, one cannot equate the participating employer with the founder of a trust. Thus, it is inappropriate to apply the principles of trust law to pension funds in the South African context.

24. Finally, some reliance was placed on the doctrine of legitimate expectation. It was claimed in argument that the complainants exited the fund on the supposition that the fund would not be subject to a radical restructure and that the employer would have no entitlement to share in the surplus. When those suppositions altered, the complainants legitimately acquired a renewed expectation to additional benefits. No factual foundation has been laid to support the existence of the alleged suppositions or their legitimacy. That aside, it is something of a long stretch to suggest that former members hold a legitimate expectation enabling them to restrain the fund from restructuring its benefit design (in accordance with the wishes of the active stakeholders) until their previously unanticipated claims, suddenly renewed, have been met, when the rules do not contemplate such a contingency.

25. Accordingly, the conclusion is inescapable that the complainants as former members have no legal rights or expectations to share in the surplus assets of the pension fund either at the time of the restructuring exercise or at any time in the future. That is not

to say that the pension fund and its board of management necessarily lack the power to benefit former members by the exercise of a discretion to enhance benefits and transfer values retrospectively. Were it shown that such a discretion did exist, then obviously it would have to be exercised properly and in a non-discriminatory fashion. It deserves to be re-emphasized that the complainants received the benefits due to them and no case has been made that their quantum was unreasonably determined at the time of withdrawal.

26. Furthermore, there is nothing in the papers before me to suggest that the fund failed to consider any claims of the complainants in good faith. The requirement of good faith does not compel the board to adopt any particular course in its scheme for distribution, provided it acts without ulterior motive, is suitably appraised of all relevant considerations and has excluded irrelevancies. The chosen scheme of distribution in this instance sought to reward existing members and pensioners, to whom the fund had ongoing liabilities, for agreeing to an altered basis of liability and at the same time gave the employer a defined entitlement to reserves in the defined contribution section in exchange for giving up its prerogative to a contribution holiday in the defined benefit section. It amounted to a re-alignment of existing risks and entitlements and no apparent justification existed for re-visiting the discharged liabilities of former members which had been extinguished two years previously.

27. Likewise, in relation to the second complaint, as former members of the fund to whom the fund owes no duties, the complainants have no standing to challenge the rule amendments giving the employer greater access to the surplus. Even if the rule amendments were unreasonable and illegal, the complainants have insufficient interest to a seek remedy. In *Bagnall v The Colonial Government* [1907] 24 SC 470, Innes CJ observed at 379:

> The general rule of our law is that no man can sue in respect of a wrongful act, unless it constitutes the breach of a duty owed to *him* by the wrong-doer, or unless it causes *him* some damage in law. This principle runs through the whole of our jurisprudence.

28. Accepting that the fund has discharged all its liability towards the complainants, it cannot be said that the complainants have any direct or sufficient interest in the affairs of the fund allowing them to challenge the reasonableness or otherwise of a rule amendment. Moreover, without deciding the point, the fact that the new rules permit the employer access to the surplus credited to the reserve account without the consent of the board and the actuary need not of itself render the rule unreasonable or illegal. In a defined benefit fund the actuarial assessment is an effective safeguard for ensuring the overarching liability of the employer to meet the balance of the cost of the benefits. Similar considerations do not apply in a defined contribution situation since the surplus has concretized and the actuary has played his role. The transfer to the reserve account replaces the employer's lawful claim to a contribution holiday in the over funded defined benefit section.

29. In reaching these conclusions, one is naturally conscious of the legitimate sense of grievance felt by former members in general about their exclusion from the distribution of surplus assets by defined benefit pension funds. In the restructuring arrangements which took place in the late 1980s and early 1990s many pension fund members left funds with benefits which might be described as less than generous. A withdrawal benefit in the amount of the actuarial reserve, as in this case, can be a generous benefit. Nevertheless, members of well funded pension funds frequently did not receive any benefit of the provision held as an investment reserve. With the benefit of hindsight, the restructuring of the industry could have benefited from better legislation and more effective regulation. As is well known, legislation has been formulated which seeks to redress some of the past inequities. Any fund, including the respondent, which has an existing surplus at the next valuation will be compelled to devise a reasonable and equitable scheme for the appropriation and distribution of any remaining surplus and will have to do so taking into account the interests of former members. The proposed legislation (as it currently stands) will compel an appropriation of the amounts credited to the employer reserve account and this may well result in some benefit for the complainants. Moreover, the proposed legislation will grant the complainants statutory rights in equity along similar lines to those

unsuccessfully asserted in his complaint.

30. However, for the reasons outlined, the complainants have no legal rights to an enhancement of the benefits which they received, nor do they have the necessary standing to challenge the rule amendments enacted some time after the termination of their membership. Accordingly, the complaints are dismissed.

Dated at **CAPE TOWN** this 31st day of March 2001.

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John Murphy
Pension Funds Adjudicator