IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO.: PFA/KZN/25/98

In the complaint between:

The Group of Concerned SAPREF Pensioners — Complainant

and

The SAPREF Pension Fund — First Respondent

Shell and BP South African Petroleum Refineries (Pty) Ltd — Second Respondent

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

The complainant is a voluntary association of pensioner members of the first respondent. The complainant has lodged a complaint with the office of the Pension Funds Adjudicator in terms of section 30A(3) of the Pension Funds Act of 1956.

The first respondent is the SAPREF Pension Fund, a defined benefit pension fund registered in terms of the Pension Funds Act of 1956 ("the fund"). The second respondent is Shell and BP South African Petroleum Refineries (Pty) Ltd, the main participating employer in the fund ("the employer").

The complaint raises three issues broadly related to the administration of the fund and the interpretation and application of its rules. Essentially, there are three separate complaints related to the distribution of the surplus in the fund. A fourth complaint concerning the election of members of the fund's management committee was also lodged, but subsequent events have led to the complainant abandoning its request for relief in this regard.

A hearing was held at the premises of the South African Petroleum Refineries (Pty) Ltd in Durban on 12 August 1998. Neither party was legally represented. No evidence was

led. The complainant's case was presented by Mr Andreas and Mr Russell. The first and second respondents' case was presented by the principal officer, Mr M Farquharson and Mr Scaife, the financial director of the employer and one of the members of the management committee.

Having considered the written and oral submissions of the parties, I have determined the complaint as follows.

Background to the complaint

Although the complainant has not formulated its complaints, and the concomitant relief sought, with the precision that one might have preferred, it is clear that the complainant seeks relief directing the fund to a particular course of conduct in the distribution of the surplus in the fund. In some respects the complainant's request for relief is somewhat premature in that no final decision has been taken about the application of the surplus. Nevertheless, the employer has had the benefit of a so-called contribution holiday and part of the surplus has been applied to augment pension benefits. It is hoped that the directions set out herein will be of assistance to the parties in the negotiation process envisaged for the further distribution of the surplus.

The first respondent, as stated, is a defined benefit pension fund which was established on 1 July 1975. The fund became closed to new membership with effect from 1 March 1995. As at 1 January 1995 the fund had 900 active members. At the time of this determination, there remain few active members in the fund. During the course of 1995 - June 1998 most of the active members of the fund moved either to the SAPREF Provident Fund or the Chemical Industrial National Provident Fund. Following the restructuring the fund has 20 active members and 263 pensioner members. Besides the pensioners and active members there are approximately 282 beneficiaries of the fund, who are either widows or orphans.

The fund is administered by a Committee of Management consisting of at least four persons, all of whom are appointed by the employer in terms of rule 7. The Managing Director of the employer acts as chairman of the committee and in terms of rule 9(2) effectively can veto any decision of the committee. Because of the 1996 amendments

to the Pension Funds Act requiring 50% of boards of management to be elected by the members of a fund before December 1998, these arrangements are currently under review and it is anticipated that a newly elected committee will be in place before 4 November 1998. The complainant originally sought relief to expedite this process. As satisfactory progress has been made in the arrangements for the election, the complainant no longer feels the need for my intervention.

At 31 December 1996 there was an actuarial surplus in the fund of approximately R193 million. The accrued funding level, that is the ratio of the fund's asset value to that of its accrued liabilities, was approximately 239% at 31 December 1996 compared to 140% at 31 December 1994. The level of funding was 278% if the market values of assets were used. According to the 1996 actuarial valuation report, the main reason for the increase in surplus was that the actual investment return exceeded the assumed investment return.

Given the favourable funding level, the participating employer in the fund, Shell and BP South African Petroleum Refineries (Pty) Ltd, has been on a so-called contribution holiday since 1 September 1994. The total value of the contribution holiday for the period to date is R4.9 million. It is provisionally estimated that a contribution holiday for the total remaining life of the fund will benefit the employer to the tune of R8.1 million.

Besides the contribution holiday, the participating employer also has had the benefit of a retrospective amendment to rule 15 of the fund's rules which effectively transferred liability for administration costs from the employer to the fund. The net saving to the employer is approximately R5.4 million for the period of the rule's retrospective operation. The complainant claims these financial advantages to the employer are unjustified, especially when compared to the low level of pension increases granted to pensioners.

As we shall see presently, in general terms, the relief sought by the complainant is an order reversing the financial advantages granted to the employer and a request that the pensioners be granted increases to compensate for the difference between the inflation rate and the actual pension increases of around 75% of the inflation rate in previous

years. The specifics of this relief are dealt with more fully below. However, it should be noted that to some extent the fund has met the demand for increased pensions. Nevertheless, further directions in this regard will be appropriate.

Legal principles governing the distribution of surpluses in pension funds

Before dealing with the complainant's complaints it may help to set out the basic legal principles governing the question of surplus distribution. The issues are complex and do not admit to easy resolution. Employers argue that surpluses represent over funding and should be used almost exclusively to reduce contributions or even to provide a refund to the employer. The argument essentially maintains that all surplus in a defined benefit pension fund is attributable to over contribution by the employer. Normally, depending on the rules of the fund, the rate of the employer's contribution in a defined benefit fund is determined with reference to certain assumptions made by the valuator. To the extent to which the assumptions result in the fund's assets exceeding its actuarial liabilities, the employer can be said to have contributed more than is required in terms of the rules of the fund and therefore is entitled to a contribution holiday. Members of pension funds generally view the issue differently. Active members view contribution holidays as a devaluation of their deferred pay. In the words of Richard Nobles in *Pensions, Employment, and the Law* (Clarendon Press, Oxford, 1993) 145:

> Members view contribution holidays as a devaluation of their deferred pay. If the surplus has been created by assets purchased from part of their pay, it should be used to increase their benefits. Had they known that their employer's contribution would provide a surplus at a future date, and that this surplus would be claimed by the employer, they might not have been prepared to accept that such a high percentage of their payroll should have gone into the pension fund. Pensioners, both existing and deferred, will feel that they have a very strong claim. Unless their pensions are indexed to earnings, they will have financed part of the surplus through a loss in the real value of their pensions. With existing pensioners, this occurs from the date of their retirement. With deferred pensioners, this occurs from the date of leaving service.

The leading South African case on the issue of pension fund surpluses is *Lorentz v Tek*

Corporation Provident Fund & Others 1998 (1) SA 192 (W). The decision makes a number of important legal findings in relation to surpluses. Two general governing principles emerge very clearly from the judgment. First of all, depending on the rules, the surplus in a fund normally accrues to the pension fund itself. Secondly, the trustees and the participating employer are under a fiduciary duty to apply the surplus reasonably.

In my opinion, much of the debate about "who owns the surplus" in a defined benefit pension fund proceeds on an incorrect footing. Formulating the question as such feeds into the common misperception that a surplus in all cases consists of tangible assets. As such, the question loses sight of the important fact that a surplus, particularly in ongoing pension funds, arises as a consequence of an actuarial judgment. Whether or not a surplus exists depends on the assumptions applied by the fund's actuary in determining whether there are sufficient assets to meet the fund's projected actuarial liabilities. An apparently substantial surplus in an actuary's valuation report may be significantly reduced in a subsequent report by virtue of a change in the assumptions or the non-realisation of certain of those assumptions in reality.

These considerations lead me to agree with the opinion expressed by Nobles (*op cit* 147) when he states as follows:

> One cannot simply state who "owns" the surplus, whether that surplus arises on final winding up or within an ongoing scheme. For a start, within an ongoing scheme, a surplus does not represent any particular assets. It is simply an actuarial opinion that the scheme is better funded than a particular method required. There is nothing to own. In this context one should not speak of owning the surplus, but ask who can expect to benefit from it. On final winding up, where the benefits are secured by the purchase of annuities, one has an identifiable share of assets which the different parties can claim. But even here, it is difficult to speak of the surplus being owned by a particular party, since entitlements will usually depend upon the trustees exercising, or failing to exercise, their power to augment benefits.
>
> The overall question of entitlement to surplus has been broken down into questions as

to who, in what situation, can expect to benefit from a surplus.....

Nobles' analysis accords broadly with the proposition flowing from the *Tek* decision that issues around surplus distribution are essentially issues of whether the trustees of a pension fund have properly applied their mind to the distribution and whether the discretion exercised has been exercised reasonably in the face of the competing legitimate expectations to benefit from the surplus. In a defined benefit fund those legitimate expectations pertain usually to the employer's desire to benefit from contribution holidays or refunds and the members claim for benefit increases. Proposed legislation dealing with the rights of employers to seek a refund of over contributions has been drafted by the Department of Finance. The proposed legislation imposes very stringent requirements. I shall return to this matter later.

In a paper presented to the annual conference of the Pension Lawyers Association in February 1998 titled the *Tek Judgment: An Appropriate Judicial Response to Pension Fund Surpluses*, Ms Rosemary Hunter usefully summarised the import of the *Tek* decision as follows:

1. A surplus in a pension fund has to be examined to determine its sources and one cannot proceed on the assumption that the surplus is solely due to over-contribution on the part of the employer.

2. It is wrong in principle to give the benefit of earnings from sources other than the employer over-contribution to the employer, unless the rules of the pension fund/ or legislation permits it.

3. To the extent that there has been over-contribution by an employer to a fund, the employer may seek an agreement with trustees that it be permitted to take a contribution holiday. Such a contribution holiday would not amount to a financial advantage such as that contemplated in section 1 of the Income Tax Act.

4. If a decision to take a contribution holiday is based on a surplus that

derives from a source other than employer over-contribution, the trustees will be breaching their fiduciary duties by giving the employer a financial benefit to which he is not entitled in terms of the Act or the rules of the fund. Their fiduciary duty is to meet the object of the fund namely to provide benefits to members.

5. In considering the equity of a scheme involving transferring members, the trustees should with the actuaries' assistance, safeguard the position of pensioners who remain in the pension fund and takes steps to ensure that the other liabilities of the transferor fund are funded. In addition "they may legitimately consider increases in future costs, including increases in pensions....they may consider any other factor which may enure to the benefit of the pensioners and active members of the pension fund at the time of the transfer."

6. The trustees may legitimately take the employer's financial interests into account insofar as they relate to its obligations to ensure the payment of defined benefits to pensioners who remained in the pension fund at the time of the transfer.

In *Euijen v Nedcor Pension Fund* PFA/GA/27/98 I held that in certain circumstances it may be legitimate for former members to share in the surplus. The difficulty here shall be in drawing an appropriate line of entitlement. Each case will have to be determined on its own merits and will depend on the circumstances and the requirement that justice should be done in each particular case.
Against this broad background, it is possible to assess the complaints of the complainant.

The complaints concerning the pension increases and the contribution holiday

The complainant's complaint concerning the application of the surplus is summarised in the complaint as follows:

> The approach from the trustees, the company and the pension fund auditors appears to be along the line that they can take advantage of the actuarial surplus of the fund without a commensurate consideration of the benefit expectations of the members of the fund.

Until fairly recently, the fund has tended to award annual pension increases approximating 75% of the inflation rate. During the restructuring in which most of the active members transferred to the provident funds, the pensioners all received a special, additional increase of 10%. After receiving the pensioners' complaint, the fund sought advice and were advised that it was usual for funds that were in a sound financial position to grant annual increases closer to the full inflation rate. The committee obtained the endorsement of the employer (as they are obliged to do in terms of rule 23(2)) to increase all pensions to a level calculated at 90% of the inflation rate from the date of retirement, with effect from 1 July 1998.

The consequence of this adjustment, together with the previous special increase of 10%, is that the pensions are now fully adjusted for inflation. This increase was funded from the surplus. In a letter dated 17 August 1998, addressed to me after the hearing, the complainant has conceded that these adjustments result in the pensions being fully adjusted for inflation. However, they draw attention to certain discrepancies between themselves and those active members who transferred to the provident funds and argue that a more equitable adjustment would be for the pensioners to be granted an additional 10% increase.

As already mentioned, the employer has been on a contribution holiday in respect of its contributions owing on behalf of the active members for the period 1 September 1994 to date. The complainant avers that the contribution holiday is not in accordance with the precepts laid down in the *Tek* case. The complainant also argues that the contribution holiday has not been in compliance with the first respondent's rules. In particular, the complainant argues that rule 48(2) of the rules requires the employer to give six months written notice to the committee to reduce, suspend, or terminate its contributions to the fund.

Arising out of these circumstances, the complainant has requested me to grant an order directing:

1. the employer to reimburse the pension fund in the amount to which it has benefited from the contribution holiday, namely, R4.9 million; and

2. that all current pensioners be granted increases to compensate them for the difference between the inflation rate and the actual increases of around 75% of the inflation rate in previous years; and

3. the employer to continue with the practice of granting increases at the inflation rate until such time as the surplus no longer permits this practice.

Dealing first with the question of the pension increases. As mentioned, shortly before the hearing of this complaint the employer and the fund met the demand for an inflation adjustment to date. All pensions will be inflation adjusted as of 1 July 1998.
More difficult is the question of whether I can order the fund to continue such practice in view of the substantial surplus.

The rules of the fund do not provide for mandatory benefit increases. Rule 23(2) allows for discretionary benefit increases at the instance of the employer in consultation with the committee of the fund. Rule 23(2) reads as follows:

> Subject to the payment of the Employers of such additional contributions (if any) as are certified by the Actuary to be required, the Company may direct the Committee to increase all or any of the Pensions payable under these Rules, or to pay a Pension otherwise than under these Rules, and any such increase may be removed or reduced by the Committee if so directed by the Company.

The *Tek* decision is authority for the proposition that if the power to increase benefits is held by the employer alone, or is held by the trustees but subject to a veto by the participating employer, then the employer's power must be exercised in good faith.

Considering the employer's veto in the *Tek* case, Navsa J observed:

> The fact that *Tek* is given the final say does not mean that it can act arbitrarily and only in its financial interests. I agree with Mr *Wallis* that, even if the pension fund rules are seen as contractual, then in terms of *Dharumpal's* case the employer is obliged to act in good faith. In *Thrells'* case the Court, in my view, correctly took into account as background or as contextual that the pension fund is an integral part of the employer/employee relationship. The respondents themselves recognise that the trustees owe the pension fund members a fiduciary duty. *Tek,* when it has the final word on the discretionary benefits, must, in my view, act in a *bona fide* manner. This it does not do when it makes the discretionary benefits illusory and nullifies a pension fund rule. It acts improperly when it does not give effect to the pension fund's objects. It does not do so when it uses pension fund assets to its own advantage. *Tek* and the trustees, in my view, misconstrued the pension fund rules and misconceived their powers and duties. (@ 229 H - 230A)

In *Mettoy Pension Trustees Ltd v Evans & Others* [1991] 2 All ER 513 @ 550G, Warner J remarked:

> In my opinion it is not correct to say that the rights of the beneficiaries under the scheme are satisfied when they have received their mandatory benefits and that anything more lies in the bounty of the employer. I think the beneficiaries have a right to be considered for discretionary benefits.

In short, the discretion conferred on the employer in terms of rule 23(2) to consider increasing pension benefits is a fiduciary duty which has to be exercised properly. The pensioners have a concomitant right to be considered for discretionary benefits.

It does not follow that any court or adjudicator without more should require the employer to grant pension increases which will increase the employer's immediate funding burden. Nor are the courts likely to require increases which will increase the employer's funding burden in the future by holding it to set patterns of increases. Disputes about pension increases and contribution holidays, in the absence of a clear statutory or contractual right to an increase or a holiday, can be classified as disputes of interest.

Unlike disputes of right, disputes of interest concern the creation of new rights, such as disputes over wage increases or the modification of contractual rights, or even the amendment of pension fund rules. Disputes of right, on the other hand, concern the infringement, interpretation and application of existing rights embodied in contracts, statutes or rules. Collective bargaining, negotiation, mediation and joint problem solving are the preferred methods for resolving disputes of interest, while adjudication is normally considered the appropriate method for resolving disputes of right. Consequently, the role of an adjudicator in this area is limited generally to acting as the custodian of the *process* whereby new entitlements are concretised through negotiation and ultimately agreement. Normally, an adjudicator will hesitate to set the substantive terms of the outcome of a negotiation. This, as a general rule, will be left to the respective bargaining power of the parties. Powers, discretions, rights and duties brought to bear in the process nevertheless have to be exercised reasonably and fairly.

This pluralistic framework ought not to be applied mechanistically. The distinction between disputes of right and disputes of interest is not hermetically sealed. - see *Metal & Electrical Workers Union of SA v National Panasonic Co* (1991) 12 *ILJ* 533 (C) @ 537 E - F. The categorisation has been described as more analogous to a semi-permeable membrane through which disputes that are normally of one type may pass and be handled by procedures usually reserved for disputes of the other. This will be especially so in disputes of interest where the bargaining power of one party is totally out of equilibrium with the other, for instance by virtue of a lack of organisation, or the incapacity to invoke equal weapons of last resort, with the result that the outcome of negotiations yields a manifestly unjust result, or one at variance with the prevailing social *mores*. In which event, judicial intervention may be justified to strike the appropriate balance in the substantive outcome. Much will depend on the circumstances.

At the very least, therefore, in this matter, the employer and the committee can be expected to exercise their discretion properly on an annual basis. Where there is a substantial surplus, as in this case, it is indeed questionable whether a pension increase in the amount of the inflation rate will be sufficient compliance with the fiduciary duty to

distribute the surplus reasonably. When dealing with a fund which is closed to new members and so well funded that the fund's actuary has concluded that future contributions from the employer are unlikely in the foreseeable future, there is more than an argument for greater generosity towards the pensioners.

The committee and the employer have indicated that they are prepared to consider annual increases in excess of the practice of granting annual increases which approximate 75% of the inflation index. This will involve utilising a part of the surplus to grant such additional amounts. However, they express the legitimate caveat that the majority of former active members who transferred to the two provident funds, were possibly under the impression that the established level of annual pension increases would remain at 75% for a considerable period. If they were aware that part of the surplus was to be used to grant bigger pension increases, many of the transferred members may have elected to remain in the pension fund. The committee recognises, therefore, that the former transferred members also have a keen interest in benefiting from the utilisation of the surplus. In recognition of the former members' potential interest (and presumably taking account of the *Tek* decision), the employer and the fund have adopted a conservative approach in relation to granting pension increases.

Additionally, the fund has indicated that it is awaiting the outcome of the election of a new board of trustees before engaging in further negotiations or decision-making in relation to the distribution of the surplus. With effect from 15 December 1998, all management boards of pension funds have to provide for 50% representation by member elected trustees. The fund anticipates a new committee being elected during September or October 1998 with the first board meeting of the newly elected board being scheduled for 4 November 1998. It is anticipated that the surplus and the question of its distribution will be further discussed at that meeting.

Hence, I am satisfied that the fund and the employer's decision to adjust pensions to take account of the inflation rate was exercised in good faith and is reasonable in the circumstances. Although the size of the surplus may have justified greater generosity, given the competing interests and the state of transition in which the fund finds itself, I

believe the conservative approach adopted is justifiable. As far as future increases are concerned, they too shall fall to be tested in accordance with the requirements of good faith and reasonableness. At which point, the negotiations around the surplus will be more advanced, and it will be easier to review the increases in the light of the outcome of those negotiations.

Turning now to the question of the employer's contribution holiday. According to the *Tek* decision, the surplus in the fund has to be subjected to a source of surplus analysis. This has not happened in this case. The purpose of an analysis is to ensure that the employer takes a contribution holiday only to the extent that there has been over contribution by the employer. If a decision to take a contribution holiday is based on a surplus that derives from a source other than an employer over contribution, the trustees will be breaching their fiduciary duties by giving the employer a financial benefit to which it is not entitled in terms of the Act or the rules of the fund. In other words, the employer has no automatic entitlement to the portion of the surplus attributable to windfalls occasioned by extraordinary returns unrelated to the employer's contribution obligation.

In the absence of an analysis of the source of surplus, it is extremely difficult for me to determine whether the contribution holiday of R4.9 million in this matter falls within the law or not. On the other hand, where a surplus of R192 million exists it seems relatively safe to assume that the employer will be able to justify a contribution holiday in the amount of R4.9 million. For that reason, I hesitate to make an order directing the employer to reimburse the contributions until such time as an analysis of the source of surplus has been done, especially in circumstances where the governance of the fund is undergoing transition and where negotiations in relation to the surplus are envisaged. Be that as it may, an order directing the management committee of the fund to obtain an analysis of the source of surplus from their actuaries will not be out of place and should serve the interests of all parties concerned for the purpose of future negotiations. It shall be so ordered.

In passing, it should be mentioned that Judge Navsa's view in *Tek* on the employer's

entitlement to contribution holidays is highly controversial. The rate of the employer's contribution in a defined benefit fund is determined with reference to certain assumptions made by the actuary. To the extent to which the assumptions result in the fund's assets exceeding it actuarial liabilities, the employer can be said to have contributed more than is required in terms of the rules of the fund. In the present matter, rule 23(1) defines the employer's obligation to make contributions in the following terms:

> Each employer shall contribute such percentage (if any), of its Members' Pensionable Salaries and such further amounts (if any), as the Actuary from time to time advises the Committee are necessary to maintain the solvency of the Fund.

A proper interpretation of this obligation might very well construe the employer's contribution obligation to be no more than to keep the fund's assets and liabilities balanced, and to absorb the effect of actual experience differing from that of the fund's actuary when performing his various calculations. In terms of this rule the actuary may very well be entitled to recommend that the employer make no annual contributions. Given that the rule is at the heart of the defined benefit arrangement it is unlikely to be considered unreasonable. On the other hand, even were one to accept this actuarial argument, there may be some circumstances in which a contribution holiday could amount to a breach of the employer's duty of good faith - see *Stannard v Fisons Pension Trust Ltd* [1992] IRLR 27 @ 32. This is less likely where there is a substantial surplus, a small active membership and a fund closed to new members.

The complainant's complaint is not restricted to the fact of the contribution holiday, but also goes to the manner in which the holiday was taken. In particular, it alleges that the contribution holiday was not in compliance with rule 49(2) of the pension fund's rules, requiring the employer to give six months' notice. Rule 49 reads as follows:

> EMPLOYER'S CONTRIBUTION REDUCED, SUSPENDED OR TERMINATED
>
> (1) All the Employers may, on giving six months' written notice to the Committee, reduce, suspend or terminate their contributions to the Fund. In the event of a notice of termination, the Committee shall, on the expiry of the period of notice determine the Fund in accordance with sub-section (1) of Rule 48. In the event

of a notice of reduction or suspension of contributions, the Committee, on the advice of the Actuary, shall make such alterations to benefits and/or contributions in respect of such Employers and the Members employed by it as it shall deem necessary or expedient.

(2) Any Employer may, on giving six month's written notice to the Committee, reduce, suspend, or terminate its contributions to the Fund. In the event of a notice of termination, the Committee shall, on expiry of the period of notice, liquidate that portion or the Fund in accordance with sub-section (4) of Rule 48. In the event of a notice of reduction or suspension of contributions, the provisions of sub-section (1) of this Rule shall, mutatis mutandis, apply.

The complainant argues that the employer may only reduce or suspend contributions on six months' *written* notice to the committee of the fund. The fund concedes that written notice was not given but argues that contribution holidays are not governed by rule 49 but rather by rule 23(1) where the actuary has determined the rate above zero. It argues that rule 49 is applicable only when the employer wishes to reduce its contribution below the level determined by the actuary in terms of rule 23(1), because it is only then that there is a likelihood of benefits being affected. Rule 49 does not apply in circumstances where the employer contribution rate is being adjusted by the fund in accordance with rule 23(1).

The wording of rule 49 clearly anticipates unilateral action by the employer to reduce contributions below the rate set by the actuary. This is very different from an adjustment of the contribution rate (even to a rate of zero) made by the fund via its actuary in terms of rule 23(1). The level at which the employer contributes has no direct bearing on the benefits members are entitled to receive in terms of the rules. This means, in a defined benefit fund, that where the employer contribution rate is set at zero it will have no detrimental effect on the members' rights. Rule 49 governs the situation where the employer seeks to reduce a rate set by the actuary other than zero, in which case members may very well be prejudiced and notice to the committee is consequently properly required. For these reasons I accept that the rule 49 has no application to the present matter.

Thus, applying the *Tek* decision, the only question is whether the employer is entitled to the contribution holiday on the grounds and to the extent of its over contribution. This can only be determined properly once an analysis of source of surplus has been completed. The appropriate relief is to direct the management committee to obtain an analysis of the source of surplus for consideration at the first meeting of the newly constituted board on 4 November 1998. In the event that the analysis reveals that the employer has been enriched unjustifiably, the complainant can approach this tribunal on the same papers for supplementary relief. The order I propose to make will facilitate such an application.

The retrospective rule amendment - indirectly accessing the surplus

The complainant complains that the retrospective amendment to rule 15 of the first respondent's rules is unreasonable, because it has allowed the employer unilateral access to the surplus.

Rule 15 in its original form read as follows:

> ADMINISTRATION EXPENSES
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> No Committee member who is in the employment of an Employer shall receive any remuneration from the Fund. Committee members who are not in such employment shall receive such remuneration as shall be determined by the Company from time to time, which shall be paid by the Employers in such proportions as the Company shall determine. All expenses incurred by the Committee in the administration of the Fund, including the remuneration of and any expenses incurred by any servant, officers, delegates, agents or nominees of the Committee, shall be reimbursed to the Fund by the Employers in such proportions as they shall agree, or, in default of agreement, as the Actuary shall certify.

On the 8 November 1996 the committee adopted a resolution amending rule 15. The resolution was adopted in accordance with the applicable rule (rule 51), in concurrence

with the participating employer, after consulting the actuary, and was made retrospective to 1 January 1995. The amended rule 15 reads as follows:

> EXPENSES
>
> No Committee Member who is in the employment of an Employer shall receive any remuneration from the Fund. Committee Members who are not in such employment shall receive such remuneration from the Fund as shall be determined by the Committee from time to time. The whole of the expenses of the Fund shall be paid by the Fund.

The resolution records that the reason for the amendment is to make the fund, instead of the employer, responsible for all the fund's expenses.

The manner in which this rule amendment came into existence appears from the correspondence submitted with the complaint.

On 21 October 1996 Mr H Buys, on behalf of the complainant, addressed a letter to the board of trustees of the first respondent. In it he comments as follows:

> With regard to the amendment of pension fund rules, we wish to point out that, contrary to present rule number 15, your annual SAPREF pension fund account report dated December 1995 stated that administrative expenses to the amount of around R2481000 charged to the fund rather than being paid for by the employers. Will rule number 15 be amended accordingly or was the item entered incorrectly?

In earlier correspondence, the complainant expressed the concern that it was not being properly advised of rule amendments. It would appear that prior to Mr Buys' letter of 21 October 1996 there had been no discussion of any amendment of rule 15.

On 22 November 1996 the principal officer of the fund, Mr Farquharson addressed a letter to Mr Buys. Regarding rule 15 he comments:

> Finally, I confirm that rule number 15 is in the process of being amended retrospective to 1 January 1995 so that the fund will bear all administration costs. We have not yet

> received confirmation of the completion of registration by the Financial Services Board but will advise all members and pensioners as soon as that has been obtained.

It will be noted that the resolution to amend rule 15 retrospectively was effected some two and a half weeks after Mr Buys wrote his letter to the committee and that the complainant was advised of the resolution some two weeks after it had been effected.

On 11 March 1997, Mr Andreas on behalf of the complainant, addressed a further letter to the committee and requested an explanation as to why the fund had deemed it necessary to amend rule 15 and why it had implemented the change prior to registration by the Financial Services Board.

In response to this letter, Mr Farquharson replied on 24 March 1997:

> SAPREF company management are no longer prepared to bear the administrative costs of the SAPREF pension fund. As the fund is in a strong financial position, and is easily able to bear those costs, the trustees decided that the fund would bear those costs effective from 1 January 1995. The amendment to rule 15 was unfortunately initially overlooked. This has now been done and registered by the Financial Services Board. In terms of section 12(4) of the Pension Funds Act, the effective date remains 1 January 1995.

On 9 April 1997 Mr Andreas addressed a letter to the Registrar of Pension Funds. In it he remarks:

> We hereby forward to you a copy of the reply, dated 24 March 1997, received from the SAPREF pension fund, from which you will note that they claim that you granted the SAPREF pension fund *post facto* approval for the implementation of the change of rule 15 of the pension fund rules. We are not aware of any members or pensioners of the fund who have consented thereto as contemplated in your Mr Cronje's faxed letter reference number 12/8/12513/1, dated 29 July 1996, to our Mr George Skinner. Your comments on the claim by the SAPREF pension fund would be appreciated.

Unfortunately, I have not been furnished with the Registrar's letter of the 29 July 1996,

nor does there appear to be an immediate response from the Registrar to this letter of 9 April 1997.

In a letter dated 11 September 1997, addressed by the complainant to the Registrar of Pension Funds, the complainant further registers its protest and request the Registrar to rescind the rule amendment. The following extracts from the letter are revealing:

> In a letter to the board of trustees dated 21 October 1996, from our group, we inter alia pointed out that, in contravention of the then present rule 15, the pension fund accounts for the year ended December 1995, stated that the administrative expenses to the amount of around R2 481 000 were charged to the fund rather than being paid for by the employers.
>
> This contravention was repeated in the accounts for 1996, as an approval from your office was only issued earlier this year. Although we are sure that it is not the intention of your board at the time, the granting of such approval with retrospective effect may possibly be construed as having condoned the wrongful actions of the trustees and/or company.

Further on in the letter, the complainant concludes:

> We believe that the company's decision, no longer to bear the administration costs and no longer to contribute towards the fund on behalf of active members of the fund, is no more than an effort on the part of the company to access the surplus in the fund without granting any substantial improvement in income to the pensioner members of the fund than had been customary in the past.
>
> In view of the aforegoing we hereby request that you rescind your decision to approve the amendment of rule 15 of the SAPREF pension fund rules, with retrospective effect and to only grant such approval with effect from 1 January 1997, at the earliest, provided you are satisfied that the company had complied with the provisions of rule 49(1) at that stage. Our preference is however in favour of complete withdrawal of the approval until such time as the election and appointment of trustees as mentioned in paragraph 5 above has been finalised.

> Should you be unable to accede to our request, it would be appreciated if this application could be forwarded to the Pension Funds Adjudicator appointed under section 30C(1) of the Pension Funds Amendment Act, 1996, for consideration in terms of section 30A of said Act.

The Registrar replied to the complainants' letter of 11 September 1997 by means of a letter dated 8 October 1997. The letter does not engage with the complainant's arguments and merely offers a brief explanation for the amendments.

As appears from the correspondence, the complainant argues that the rule amendment was unreasonable because essentially it amounted to the fund relying on its power of amendment to afford the employer access to the surplus without consultation or negotiation with the members of the fund. The complainant alleges that the members were not notified of the amendment, no opportunity was afforded to them to make submissions or representations concerning the desirability of the amendment, and the retrospective effect of the amendment has had a negative impact on their reasonable benefit expectations. The complainant places much weight on the unrepresentative composition of the committee. As stated earlier, the committee consists of four persons, all of whom are appointed by the employer.

At the hearing, Mr Russell, the former principal officer of the fund, and now a member of the complainant, made certain oral representations about the rationale for rule 15 in its original form. He submitted that the sole reason the company agreed to incur the administration expenses was to ensure that it gained appropriate tax relief for its contributions to the fund. Because of the need of the fund to finance the past service liability of black employees who had previously been excluded from the fund, the employer's contribution rate was very high and the agreement by the employer to pay the administration expenses was simply a means of obtaining the maximum taxation benefit for the contributions to the fund.

The fund, in its reply, explains that the employer is no longer prepared to pay the administration costs. It maintains that the amendment to rule 15 was unfortunately initially overlooked. However, it also makes a seemingly contradictory argument that

prior to amendment rule 15 was capable of being interpreted to mean that the fund was liable to pay the expenses in the first instance and that the employer would subsequently pay these back, or a portion thereof, at its discretion. In other words, the fund always bore the principal obligation to pay the expenses, and it was not obliged to recover these from the employer. Thus, neither the fund nor the members have been prejudiced by the retrospective amendment.

With respect, I find this argument most unconvincing. If there were no obligation on the employer to pay the expenses, there would have been no need to amend rule 15 in the first place. Moreover, the first respondent has not seriously contested Mr Russell's respresentations about the original rationale of rule 15. The final sentence of the original rule 15 is clear in its requirement that all expenses incurred by the committee in the administration of the fund *shall* be reimbursed to the fund by the employers.

In support of its argument, the fund relied on the wording "*in such proportions as **they** shall agree*" in the original rule 15 to suggest that the fund could agree with the employer to bear 100% of the costs and require a nil reimbursement by the employers. The argument is plainly without merit. The "*they*" referred to in that part of the rule is a reference to the employers in the fund. Originally there was more than one employer participating in the fund. The purpose of this provision is to allow the cost of reimbursement to be distributed amongst all the employers. It does not envisage a distribution of the cost of the expenses between the employers and the fund. According to Mr Russell the past practice was to distribute the costs proportionally among the participating employers on the basis of a head count of members employed by each employer. Prior to the amendment, the fund never contributed towards the fund's expenses. Accordingly, I am satisfied that the obligation on the employers to reimburse the fund's expenses was absolute prior to the amendment and that the fund bore no liability in that regard.

The effect of the rule amendment has been to diminish the employer's liability towards the fund considerably. The evidence suggests that for the 1995 and 1996 financial years the participating employer has made a saving of R5.4 million. As such it is fair to

say that the rule amendment has given the employer access to the surplus. The fund basically concedes this by arguing that the favourable funding position of the fund permits it to pay its own administration costs without affecting the ability to pay pensions. Moreover, it draws attention to the fact that other funds usually foot the bill for their own expenses.

Be this as it may, the issue remains whether the committee's reliance on the power of amendment to grant the employer such access to the surplus, and the consequent rule, can be considered as lawful and reasonable in the circumstances.

In *San Giorgio v The Cape Town Municipal Pension Fund* (Case no. PFA/WE/8/98) I held that, as part of a trustee's duty to act with due care and diligence, trustees of pension funds are required to exercise their powers reasonably and justifiably. A decision by a pension fund or its trustees which is unreasonable will constitute either an improper exercise of power or maladministration as contemplated in the definition of a complaint in section 1 of the Pension Funds Act. In a constitutional state with a fundamental constitution, the requirement of reasonableness introduces a test of proportionality between the objectives of a decision and the means applied to give effect to that decision. According to van Deventer J in *Roman v Williams N O* 1998 (1) SA 270 (C) @ 281 this means that judicial review is no longer limited to scrutinising the way in which an administrative decision is reached but can involve scrutiny of the substance and merits of the decision. Hence, it is permissible to look at the purpose, means and effects of both the decision to amend the rule and the consequent rule.

In this case, the decision of the committee and the consequent rule have as their purpose the abolition of the employer's pre-existing and future liability towards the fund with the effect that the assets and wealth of the fund have been diminished. In the result, the surplus of the fund has been reduced to the advantage of the employer without any consultation or negotiation with the members of the fund. As at the date of the amendment the employer owed the fund R5.4 million for administration expenses. Effectively the trustees have refunded the employer that amount. Whether such a course of conduct can be seen as reasonable depends on a number of considerations.

The starting point for determining whether the committee has acted reasonably is to consider its fiduciary duties. These derive from statute and the common law. It is not my intention to explore these in any detail. Nevertheless, it will do no harm to enumerate some of the relevant fiduciary duties to sketch the backdrop against which trustees should always act when dealing with surpluses.

The single most important duty of a management board of a pension is the duty to act in the beneficiaries' best interests. This will soon be codified for the purpose of pension funds when the amendment in section 7C(2)(a) of the Pension Funds Act becomes effective. It requires the board in pursuing its objects to take all reasonable steps to ensure that the interests of members in terms of the rules of the fund are protected at all times. In English law the duty appears to go further in that it has been held that it is not enough for the trustee to have acted in good faith, and with the intention of benefiting the beneficiaries. If it is clear to the court that the actions taken were not in the beneficiaries' best interests the courts will intervene. In *Hampden v Earl of Buckinghamshire* [1893] 2 Ch. 531 @ 544, the principle was stated thus:

> Still an honest trustee may fail to see that he is acting unjustly towards those whose interests he is bound to consider and to protect; and if he is so acting, and the court can see it although he cannot, it is in my opinion the duty of the court to interfere.

Likewise, section 7D(1)(c) of the Pension Funds Act soon will give expression to the common law duty of trustees to keep members adequately informed of their rights and benefits. Similarly, section 2(c) of the Financial Institutions (Investment of Funds) Act of 1984, prohibits a trustee from alienating the property of the trust in an manner calculated to gain any improper advantage for himself or any other person at the expense of the trust or beneficiary. Finally, there is a duty to exercise the powers of the trust in an impartial manner when choosing between the interests of different groups of beneficiaries.

As stated, I do not propose to scrutinise the first respondent's conduct in this matter closely to assess whether the amendment to rule 15 in any way was directly in breach

of these duties. I mention them merely as a backdrop to my determination of the reasonableness of the amendment. This matter was presented to me without the benefit of legal representation, and I accordingly hesitate to pronounce on issues of propriety without the benefit of further evidence and legal argument. The decision I have reached, and my reasons for it, also preclude the necessity for doing so in that the governing principles can be derived from the duty to act in good faith and the duty to act in the interests of the members.

In *Re Courage Groups Pension Schemes* [1987] 1 All ER 528 Millett J held that the purpose of a pension fund is to benefit the past and present employees of the business covered by the fund, and the powers contained within the fund's rules should not be exercised in such a manner as to defeat these purposes. Commenting on the employer's right to participate in the surplus by using the power of amendment, the learned judge commented as follows:

> It will, however, only be in rare cases that the employer will have any legal right to repayment of any part of the surplus..... Repayment will, however, still normally require amendment to the scheme and thus cooperation between the employer and the trustees or committee of management. Where the employer seeks repayment, the trustees or committee can be expected to press for generous treatment of employees and pensioners, and the employer to be influenced by the desire to maintain good industrial relations with its workforce.
>
> It is, therefore, precisely in relation to a surplus that the relationship between the company as the employer and the members as its present or past employees can be seen to be an essential feature of a pension scheme.... While [the members] have no legal right to participate in the surpluses in the existing schemes, they are entitled to have them dealt with by consultation and negotiation between their employers with a continuing responsibility towards them and the committee of management with a discretion to exercise on their behalf, and not to be irrevocably parted from these surpluses by the unilateral decision of a take-over raider with only a transitory interest in the share capital of the companies which employ them. (@ 545 - 6)

In short, while the members of pension funds do not have legal rights to participate in surpluses in an ongoing scheme, they do have the legitimate expectation that surpluses

shall be dealt with through a process of negotiation, consultation or joint problem solving. By introducing such a duty, Millett J indirectly introduced a duty to negotiate benefit increases before using the power of amendment as a means of accessing the surplus. Such a duty perhaps cannot be interpreted to impose an obligation to reach agreement. The duty is to engage in a process whereby the competing interests are adequately ventilated and taken into consideration in distributional decision making.

The power of pension funds to amend their rules in South Africa is derived from section 12 of the Pension Funds Act of 1956. Section 12(1) provides:

> A registered fund may, in the manner directed by its rules, alter or rescind any rule or make any additional rule, but no such alteration, rescission or addition shall be valid -
>
> (a) if it purports to affect any right of a creditor of the fund, other than a member or a shareholder thereof; or
>
> (b) Unless it has been approved by the Registrar and registered as provided in subsection (4).

Subsection (4) provides:

> If the Registrar finds that any such alteration, rescission or addition is not inconsistent with this Act and is satisfied that it is financially sound, he shall register the alteration, rescission or addition and return a copy of the resolution to the principal officer with the date of registration endorsed thereon, and such alteration, rescission or addition, as they case may be, shall take effect as from the date determined by the fund concerned or, if no date has been so determined, as from the said date of registration.

The fund's powers of amendment are contained in rule 51 of its rules. The rule is lengthy and complex and need not be repeated here in full. Suffice it to say that the power of amendment rests with the committee, but requires the concurrence of the employer.

In *Lintas SA Pension Fund v The Registrar of Pension Funds* (an appeal to the Appeal

Board established by section 26 of the Financial Services Board Act of 1996), the Appeal Board acknowledged that there were important limitations on the power of amendment. At page 37 - 39 of the judgment the Board observed as follows:

> On the original formulation of rule 38A a question may have arisen whether the trustees fulfilled or breached their trust obligations towards members of the fund, and, in the latter event, whether the Registrar was then not correct in refusing to approve of and register the originally proposed rule 38A. One basis for such refusal may have been that section 12(1) of the PFA provides that a registered fund may "in the manner directed by its rules" make such alteration, rescission or addition, and such rules would ordinarily authorise trustees to agree to such alteration, rescission, or addition only in the interests of the beneficiaries of the fund, and not otherwise. This approach is in keeping with the way in which the articles of companies have been interpreted in regard to the actual authority conferred upon directors of companies, namely that it is implied that the authority of directors is conferred for and confined to the exercise of their powers for corporate purposes (in contradistinction to private purposes or ulterior purposes). .....
>
> Another basis may have been that an alteration or rescission of, or addition to, the rules of a registered fund which is destructive of the fundamental objects of such fund, would not fall within the scope and meaning of the words "alter, rescind any rule or make any additional rule" used in section12(1).

Nothing explicitly in section 12 or in rule 51 of the first respondent's rules obliges a process of negotiation, consultation or decision making in effecting amendments authorising the employer access to the surplus. However, it is instructive to note that in the *Lintas* appeal, the Board was much influenced in its decision to uphold the rule amendment in that case by the fact that there had been negotiations and that the consent of the various stakeholders had been obtained.

As mentioned earlier, there exists a draft proposal for legislation, the Pension Funds Amendment Bill, dealing with the matter of refunds to employers out of surpluses. The Bill is in response to the *Lintas* appeal. While the appellant's appeal was upheld in that matter, the Board was at pains to emphasise that it was not pronouncing on the merits or otherwise of refunds to employers. It merely rejected the Registrar's reasons for refusing

to register a rule amendment.

Because of the lack of clarity, the matter was referred to the Pension Funds Advisory Committee. The proposed legislation is the result of the deliberations of a representative task group set up by the Pension Funds Advisory Committee. The task group was mandated to consider the advisability of a defined benefit retirement fund making payment of surplus fund assets to the participating employer. Before repatriation will be allowed the trustees shall be obliged to make an application to the Registrar in accordance with a rule permitting such repatriation. Generally, members will have to consent to the repatriation after full disclosure of information. Any future fund deficit will be a legal liability of the employer for a period of 7 years after repatriation of the surplus.

These safeguards reflect a legitimate and proportional response to the issue and are the product of a corporatist policy exercise at national level.

In the present matter, the evidence shows that the committee failed to communicate its decision to waive its right to obtain reimbursement of the expenses. Thereafter when it realised that a retrospective rule amendment was necessary, it failed to give notice of the rule amendment to the members, nor did it seek any input from them. The committee simply accepted the employer's dictat that it was no longer willing to meet the administration expenses. The committee, the membership of which is exclusively determined by the employer, chose to relinquish the fund's contractual entitlements and agreed to fund the pre-existing and future expenses out of the surplus. Thereby it granted the employer an indirect refund of the surplus without embarking on a process of negotiation in which fulfilment of its obligation to press "for generous treatment of the employees and pensioners". Nor were any other safeguards, of the kind envisaged by the proposed repatriation legislation, in place.

On this basis, I am of the opinion that the committee lost sight of the object of the fund, specified in rule 4, to provide benefits for past and present employees. By exercising the power in the manner that it did, it undermined that object. The decision to make the rule retrospective was made in the hope of rendering lawful conduct which was in breach of

the original rule 15.

In terms of section 12(4) of the Pension Funds Act, amendments to rules take effect as from the date determined by the fund or, if no date has been so determined, from the date of registration. In this case the fund determined the date to be 1 January 1995, being virtually two years prior to the resolution to amend. It did so in response to the complainant drawing attention to the illegality of its conduct.

Only Parliament has the power to legislate retrospectively or to authorise retrospective legislation. In *Pretorius v Minister of Defence* 1981 (1) SA 1174 (ZAD) Fieldsend C J stated the principle as follows:

> It is an accepted principle that subordinate legislation cannot, without express power in the empowering legislation, alter or amend a right conferred by that legislation.

In *R v Selikman* 1924 TPD 650 a full bench held that the determination of a minimum wage by a wage board with retrospective effect was invalid for want of authorisation by the enabling statute.
These authorities compel me to investigate whether section 12 of the Pension Funds Act empowers a pension fund to alter or amend rights conferred by the rules of a fund retrospectively. The section must be interpreted with due consideration for the presumption against retrospectivity. A law is presumed not to be retrospective unless such was clearly the intention of the legislature. The presumption is a fundamental principle of the *rechtstaat* and a safeguard against arbitrary power being applied to subvert vested rights.

As mentioned, section 12(4) provides that amendments shall take effect either from the date determined by the fund, or if no date has been determined by the fund then from the date of registration. The Registrar takes no decision in that regard. It is the pension fund which determines the date. Yet, the provision does not empower funds to set retrospective dates for amendments. There is nothing express to that effect and nor is it the necessary implication of the section. There is no clear indication in section 12(4) of a legislative intention to give such an extensive power to pension funds. In granting

pension funds the power to set a date other than the date of registration, in the absence of a clear indication that such power can be exercised retrospectively, section 12(4) restricts the fund to rendering the amendment effective on a date between the board's resolution to amend and the date of registration, or alternatively on a date after registration.

Even were section 12(4) capable of a construction authorising pension funds to make retrospective amendments, that in itself would not preclude any investigation of the reasonableness or constitutionality of such a retrospective amendment. In determining the reasonableness of a retroactive measure, the courts, including the Adjudicator, are entitled to weigh the nature and extent of the public interest served by its retroactivity, the extent to which it modifies or abrogates any pre-existing vested rights and the nature of the vested rights which have been altered. The decisive factor is the importance of the public interest served and the extent to which that end can be implemented only by retrospective action impacting on pre-existing rights.

In my view, the retroactive operation of the amendment cannot be justified in this case. Alternative options were available to the employer and the fund. Stripped to its essence, it is clear that what the amendment hopes to achieve is unilateral access to the surplus by the employer. A more suitable and better alternative would have been for the committee to have required the employer to embark on a process of negotiation or consultation for the purpose of determining the various interests and entitlements to share in the surplus. Such a course of conduct would have been in keeping with the convictions (*boni mores*) of the pensions community on the issue, as reflected in the proposed legislation.

For the aforegoing reasons, I am satisfied that the retrospective amendment of rule 15 by the management committee was both unlawful and unreasonable.

In relation to the employer's prospective obligation to pay future fund expenses, the employer ought to have given reasonable notice (or notice in terms of rule 49 of the fund's rules - if applicable) of its intention to suspend these payments. The complainant

accepts that the employer has the right to terminate payment of the fund's expenses on reasonable notice and seems willing to waive its right to proper notice. For that reason it seeks relief only in respect of the retrospective application of the amendment.

The appropriate remedy, therefore, is to sever the portion of the amendment which is unlawful, unreasonable and contrary to public policy, namely its retrospective operation. I am guided in this respect by the test formulated in *S v Prefabricated Housing Corporation (Pty) Ltd* 1974 (1) SA 535 (A). Where it is possible to separate the good from the bad in a statute and the good is not dependent on the bad, then that part of the statute which is good must be given effect to.

A decision to set aside the effective date of a rule amendment registered in terms of section 12 of the Pension Funds Act raises questions about my jurisdiction and powers to do so.

In *Meyer v Iscor Pension Fund* (Case no. PFA/GA/6/98) I held a complaint that a rule is invalid on the grounds of public policy (*contra bonos mores*), unreasonableness or unconstitutionality is a complaint which relates to the interpretation and application of the rule alleging a dispute of law. As such, the complaint falls within the definition of complaint in section 1 of the Pension Funds Act. The definition determines the parameters of my jurisdiction and it is a requirement that the complaint should relate to the administration of a fund, the investment of its funds or the interpretation and application of its rules. A complaint alleging invalidity requires the interpretation of the rule's purpose and means to determine its consistency with the principles of the *Rechtstaat*. In reaching this conclusion one needs to explore what is meant by the term "*the interpretation and application of its rules*" in the definition of a *complaint* in section 1 of the Pension Funds Act.

Twining and Miers, *How to do things with Rules* (Weidenfeld and Nicolson, London 1976), explain the term "interpretation" as follows:

> The word 'interpretation' has various shades of meaning; in respect of rules, 'to interpret' is generally used in the sense of 'to clarify the scope of' or 'to attribute a meaning to' a

> rule or part thereof. In some contexts it can be treated as being synonymous with such words as 'elucidate', 'explain' or 'construe', all of which suggest that the subject-matter has an established or settled meaning which it is the role of the interpreter to search for, discover and bring to light, as in a hunt for buried treasure. But often the word 'interpret' is used to suggest a wider role for the interpreter, one that involves an element of elaboration or choice or even of creation. Typically it calls for exercise of the elusive quality of 'judgment'. Thus the 'buried treasure' analogy is inappropriate in the context of Olivier's interpretation of Hamlet, or Brendel's interpretation of a Beethoven sonata, or a Muslim theologian's 'free' interpretation of the Koran *(ijtih~d)*. In such contexts it would seem odd to treat interpretation as solely a matter of explanation or discovery; the interpreter is working with material that offers a greater or lesser degree of scope for choice and intervention on his part.

Interpretation refers thus to the clarification of the *general* scope or meaning of a rule. *Application* refers to applying the rule concretely to the facts of a particular case. Questions concerning the validity of a rule involve making choices about the consistency of a rule's objective and means with the constitution, statutes or the norms of public policy and reasonableness. A complaint about validity therefore relates to both the interpretation and application of the rule and involves a dispute of law about the reach of a chosen interpretation.

Furthermore, section 30E(1)(a), granting me the power to make the order which any court of law may make, in my view, permits me to declare rules of pension funds invalid on the grounds of unreasonableness or unconstitutionality. The subsection gives me powers equivalent to a High Court judge whose powers unquestionably extend to striking down invalid subordinate legislation or contractual terms.

It may be argued that section 30D read with section 30A of the Pension Funds Act, 24 of 1956, provides that the main object of the Adjudicator is limited to disposing of complaints between a fund and its members as well as any participating employer, and this excludes complaints against decisions of the Registrar to register a rule amendment.

Section 30D of the Pension Funds Act reads as follows:

The main object of the Adjudicator shall be to dispose of complaints lodged in terms of Section 30A(3) of this Act in a procedurally fair, economical and expeditious manner.

Section 30A reads as follows:

(1) Notwithstanding the provisions of the rules of any fund, a complainant shall have the right to lodge a written complaint with a fund or an employer who participates in a fund.

(2) A complaint so lodged shall be properly considered and replied to in writing by the fund or the employer who participates in a fund within 30 days after the receipt thereof.

(3) If the complainant is not satisfied with the reply contemplated in subsection (2), or if the fund or the employer who participates in a fund fails to reply within 30 days after the receipt of the complaint the complainant may lodged the complaint with the Adjudicator.

I cannot agree that section 30A can be construed to limit my jurisdiction to disposing of complaints between a fund or a participating employer and its members. The true jurisdictional precondition is contained in a definition of a complaint in section 1 of the Act which requires the complaint to relate to the administration of the fund, the investment of its funds or the interpretation and application of its rules.

The purpose of section 30A is to establish a mechanism for the submission of complaints. The fact that the initial complaint has to be lodged with the fund or the employer does not of itself limit my jurisdiction in respect of the subject matter of complaints or the parties. My jurisdiction over subject matter, as I have said, is determined principally with reference to the definition of a complaint and not a procedural provision with the primary purpose of facilitating a narrowing of the issues and setting time limits for the lodging of the complaint. An attempt to limit the object of the Adjudicator with reference to the procedural provisions of section 30A would unduly restrict the Adjudicator's powers and is not supported by a reading of Chapter VA as a whole. Thus, section 30G makes it plain that persons other than the fund or an employer can be made party to a complaint. Section 30G of the Pension Funds Act reads as

follows:

> The parties to a complaint shall be -
>
> (a) the complainant;
>
> (b) the fund or person against whom the complaint is directed;
>
> (c) any person who has applied to the Adjudicator to be made a party and who has a sufficient interest in the matter to be made a party to the complaint;
>
> (d) any other person whom the Adjudicator believes has a sufficient interest in the matter to be made a party to the complaint.

Similarly, section 30F provides that the Adjudicator shall afford the fund "*or person against whom the allegations contained in the complaint are made*" the opportunity to comment on the allegations. It would seem to me that there would be no point in allowing the Adjudicator to join parties other that pension funds and participating employers were it not possible to grant relief against such persons. And presumably, the legislature intended the Adjudicator to grant relief against such parties in those instances where their conduct falls within the definition of a complaint.

Concededly, section 30A(2) seems to contemplate that the jurisdiction over parties is limited to the complainant, the fund and the employer. But this is plainly at odds with section 30F and Section 30G which contemplate other parties in the proceedings before the Adjudicator. Insofar as the provisions seem to be inconsistent it needs to be remembered that section 30A(2) governs the internal dispute resolution proceedings of the fund and employer. Sections 30F and 30G apply to proceedings before the Adjudicator. Section 30A(2) thus recognises the obvious reality that parties other than the fund or employer cannot be brought to account in the internal proceedings. Should the complaint in the internal proceedings reveal the need to join external parties before resolution is possible, such will have to be stated by the fund or the employer in the section 30A(2) reply. In which event, if the external party is unamenable to settlement by agreement, the appropriate mechanism of supervision and enforcement is the

Adjudicator, once a complaint has been lodged under section 30A(3) and the external party is cited by the complainant in terms of section 30G(b) or is joined by the Adjudicator under section 30G(d). Thus, in my view, depending on the circumstances, it is conceivable that the Registrar could be a party in proceedings before the Adjudicator. As we shall see presently, there is no need for the Registrar to be a party in the present proceedings.

Before registering a rule amendment, the Registrar has to find that the amendment is not inconsistent with the Act and has further to be satisfied that it is financially sound. Should he make these two findings, he is obliged to register the amendment. Rules once registered have binding effect in the limited manner provided in terms of section 13. Section 13 provides:

> *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 of whose claim is derived from a person claiming.

The words "subject to the provisions of this Act" are important. In the majority judgment in *S v Marwane* 1982 (3) SA 717 (A) at 747H - 748B, Miller JA explained that the purpose of the phrase "subject to" when used in a legislative provision, is:

> "....to establish what is dominant and what subordinate or subservient; that to which a provision is "subject", is dominant - in case of conflict it prevails over that which is subject to it. Certainly, in the field of legislation, the phrase has this clear and accepted connotation. When the legislator wishes to convey that that which is now being enacted is not to prevail in circumstances where it conflicts, or is inconsistent or incompatible, with a specified other enactment, it very frequently, if not almost invariably, qualifies such enactment by the method of declaring it to be "subject" to the other specified one. As Megarry J observed in *C and J Clark v Inland Revenue Commissioners* [1973] 2 All ER 513 at 520:
>
>> In my judgment, the phrase "subject to" is a simple provision which merely subjects the provisions of the subject subsections to the provisions of the master subsections. When there is no clash, the phrase does nothing: if there is

> collision, the phrase shows what is to prevail."
>
> But when the intention is that that which is now being enacted shall prevail over other laws or provisions which may be in conflict with it, it is almost invariably prefaced by a phrase such as "notwithstanding any contrary provision...." or words to similar effect...."

The effect is that where rules are inconsistent or incompatible with other provisions of the Act, the other provisions prevail over section 13 and the rules. Rules consequent upon an abuse of power or maladministration do not enjoy binding effect because that effect would be incompatible with the provisions of Chapter VA of the Act aimed at empowering the Adjudicator to reverse abuses of power and maladministration in the affairs of pension funds. In this regard, it should be remembered, there exists extensive relief against the Adjudicator's decision in terms of section 30P of the Act.

Some argument may be made that the complainant's correct remedy should have been to lodge an appeal in terms of section 26(2) of the Financial Services Board Act, 97 of 1990, against the Registrar's decision to register the rule amendment. Section 26(2) reads as follows:

> Any person aggrieved by a decision of the Executive Officer under a power conferred or a duty imposed upon him by or under this Act or any other law may within the period and in the manner and upon payment of the fees prescribed by the Minister by regulation, appeal against such decision to the Board of Appeal.

However, this complaint does not involve a review of any decision by the Registrar. The complaint here is limited to an objection to the retrospective date of the amendment. The complaint is not about the registration of the amendment. The *decision* to make the amendment retrospective was a *decision of the fund*, not the Registrar. The effective date of an amendment is a date determined by the fund, or if no such date is determined, the date of registration. It follows that the complainant could not rely on the provisions of section 26(2) of the Financial Services Board Act to remedy its grievance about the effective date because it cannot be said to be a "*person aggrieved by a decision by the Executive Officer*" simply because there is no decision of the Executive Officer which

aggrieves him.

The appeal to the Appeal Board against the Registrar's decision to register a rule amendment is in any event limited to testing the rule's consistency with the Act and its financial soundness. In the *Lintas* appeal discussed above, the Appeal Board rejected an argument by the Registrar that the Registrar was entitled to refuse to approve and register an alteration or rescission of or an addition to the rules if he considers it to be against the public interest. The Board held that the absence of any reference to the public interest in sections 12(1) and 12(4) signifies that the test of the public interest does not arise in connection with an exercise of the Registrar's powers and duties under section 12. By limiting itself in this way, the Board presumably would also hesitate to bring reasonableness into account because there is no reference to such criteria in section 12.

Complainants' rights under Chapter VA of the Pension Funds Act (dealing with the consideration and adjudication of complaints) go further than testing a rule's consistency with the Act and its financial soundness and would allow for considerations of the public interest and reasonableness to be brought into account. Because it is unnecessary to pronounce on the issue in this matter, I leave open the question of whether the Adjudicator is empowered to pronounce upon a rule amendment's consistency with the Act, or its financial soundness; or whether that falls within the exclusive domain of the Appeal Board. Suffice it to say: it would seem unusual for an adjudicator to be required to enforce a registered rule which is objectively unlawful.

However, as I have stated, I am satisfied that complainants have a right to seek appropriate relief under Chapter VA in disputes of law about the interpretation and application of pension fund rules requiring the testing of a rule's consistency with the Constitution, the common law doctrine of reasonableness, and most probably the Act. Were I not possessed of this jurisdiction, it would mean, by virtue of the *Lintas* appeal, that members would have no protection against unreasonable rules. Neither the Adjudicator nor the Appeal Board could come to an aggrieved member's assistance. The amendments introducing Chapter VA were enacted after the *Lintas* appeal and, for the reasons mentioned, it would seem the legislature intended to grant jurisdiction over

these matters, in the first instance, to the Adjudicator, with a right of appeal or review to the High Court in terms of section 30P.

This interpretation of section 12(4) of the Pension Funds Act, read with section 26(2) of the Financial Services Board Act, leads us to the rather awkward conclusion that the Appeal Board and the Adjudicator have a concurrent jurisdiction over rule amendments. Alternatively, the jurisdiction is divided between the two bodies depending on the cause of action. Plainly the situation is not entirely satisfactory and Parliament may need to give consideration to an appropriate amendment to the legislation streamlining the adjudication process.

In setting aside as *ultra vires* the effective date of the amendment determined by the fund, I hesitate, in the interest of certainty and finality to refer the question back to the fund. Fairness will be sufficiently served if I substitute my decision for that of the committee, and with due regard to section 12(4) declare the amendment to take effect as from the date of registration.

In the final analysis, the reversal of the effective date of the rule amendment results in the second respondent being indebted to the first respondent for the fund's expenses for the period 1 January 1995 until the date of registration. Insufficient evidence has been placed before me to determine the precise amount owing. The date of registration is unknown to me, but should be ascertainable from the Registrar. I have taken account of this in granting relief.

The appropriate remedy

The appropriate relief in surplus cases is not a simple matter. The complainants have requested me to order the employer to make payment of the contributions which it has not paid while enjoying the contribution holiday, and to reimburse the fund expenses for the retrospective period of the rule amendment and at the same time to award them pension increases in keeping with their reasonable benefit expectations.

As discussed earlier in this award, many of the issues raised in this matter are of a distributional nature of the kind normally not amenable to resolution through the process of adjudication. In the main, issues related to the distribution of actuarial surpluses in pension funds are more amenable to resolution through the process of negotiation and joint problem solving. That is not to say there will be no role for adjudication in the process. The courts and judicial tribunals should act as guardians of the *process*.

What is required in this case is an order compelling negotiations involving all the interested stakeholders, including the former members of the fund who have transferred to the defined contribution funds. The aim should be to resolve all outstanding issues regarding entitlements to share in the surplus. All the interested parties are fully aware of the necessity for such a process. The negotiations can take place against the backdrop of this determination which has defined some of the parties' rights and which should serve as an incentive to a negotiated solution. The election of a representative management committee and its first meeting on 4 November 1998 presents the moment for the commencement of these negotiations.

In other circumstances, and particularly in the future when the law on the subject is more settled, it may have been entirely appropriate to set aside the employer's contribution holiday and to have ordered the employer to repay the contributions on the grounds that the contribution holiday was taken without having first obtained an analysis of the source of surplus. Likewise, it may have been appropriate to order the employer to reimburse immediately the fund expenses for the retrospective period of the amendment, which is in effect a refund or another form of contribution holiday. In this instance, and at this stage, I am reluctant to do so because of the potentially serious financial implications of such an order on the employer's cash flow, in respect of which I have no evidence, but also because of the possible adverse impact on the negotiation process that lies ahead.

Given that neither party was legally represented and neither placed appropriate evidence before me as to the financial consequences that would flow from such an order, the best solution is to compel a negotiation process which will yield the necessary evidence for determining the parties respective liabilities.

I have been guided by the order of Seady A J in *Leonard Dingler Employee Representative Council v Leonard Dingler (Pty) Ltd & Others* (1998) 19 *ILJ* 285(LC). There the learned judge postponed the proceedings and gave the parties an opportunity to remedy their differences by means of a process of negotiation.

The likely parties to such a negotiation in this case would be the fund, the employer, the complainant and the representatives of the employer's employees who may have an interest in the distribution of the surplus. Should the parties not be able to reach agreement by an appointed date, I shall finally determine the employer's liability to the fund in respect of the unpaid fund expenses and the contribution holiday (if any) and shall make an order directing payment of these amounts to the first respondent.

Should the complainant at the reconvened hearing wish to argue that I have the power to award additional pension increases, it shall be well advised to seek legal advice in order to make out a proper case setting out the basis of my jurisdiction and the power to make such award.

In conclusion, the complainant's complaint is determined on the following basis:

1. The decision of the committee of management of the first respondent of 8 November 1996 to make the amendment to rule 15 of the first respondent's rules effective from 1 January 1995 is hereby set aside.

2. The amendment to rule 15 pursuant to the decision of the committee of management is hereby declared to take effect as from the date of registration as contemplated in section 12(4) of the Pension Funds Act of 1956.

3. The second respondent is declared to be indebted to the first respondent for all the expenses incurred by the committee in the administration of the fund, including the remuneration of and any expenses incurred by any servant, officers, delegates, agents or nominees of the committee, as contemplated by Rule 15 of the first respondent's rules prior to its amendment, for the period of 1 January

1995 until the date of registration of the rule amendment.

4. The committee of the first respondent is directed to compute and determine the amount owing by the second respondent to the first respondent in respect of fund expenses payable in terms of the unamended rule 15 for the period 1 January 1995 until the date of registration of the rule amendment, together with interest at the rate prescribed in respect of a judgment debt in terms of section 2 of the Prescribed Rate of Interest Act 1975, and to present such computation to the meeting of the committee on 4 November 1998.

5. The committee of the first respondent is directed to seek and obtain from the valuator of the first respondent a comprehensive analysis of the source of the actuarial surplus in the fund for presentation to the meeting of the committee on 4 November 1998.

6. The matter is postponed until 20 January 1999 at which time this tribunal will fashion an appropriate remedy unless before that time, the parties, with or without third party intervention, reach a mutually acceptable and appropriate solution to address this complaint.

7. The parties are entitled to place further relevant evidence and submissions before this tribunal on 20 January 1999.

8. Any party is entitled to anticipate the resumption of these proceedings by giving the other parties and this tribunal 14 days notice.

DATED AT CAPE TOWN THIS 31ST DAY OF AUGUST 1998.

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John Murphy
PENSION FUNDS ADJUDICATOR