IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO.: PFA/GA/27/98

In the complaint between:

Tom Gerard Euijen

Complainant

and

The Nedcor Pension Fund

Respondent

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

Introduction

This is a complaint in terms of Section 30A of the Pension Funds Act of 1956.

The complainant lodged a written complaint on 4th March 1998 to which the respondent responded in writing on 10th March 1998. Both the complaint and the response annex detailed supporting documentary evidence.

Both parties accepted that I should treat this matter on a semi-urgent basis. Therefore, shortly after receiving the documentation in terms of the powers granted to me under section 30J of the Act, I convened a hearing at the Land Claims Court, Johannesburg on 13 March 1998. The parties consented to legal

representation and in terms of the discretion granted to me under section 30K I permitted both to be represented by counsel. The complainant was represented by Adv P Kennedy, instructed by attorneys Cheadle, Thompson and Haysom. The respondent was represented by Adv S J du Plessis SC, instructed by Cliffe Dekker & Todd Inc. No oral evidence was led and the parties relied exclusively on the documentary evidence and arguments presented by counsel.

Having completed my investigation I have determined the complaints as follows. These are my reasons therefor.

Background to the complaint

The complainant, Mr T G Euijen is a retired member of the Nedcor Pension Fund (the respondent). He was employed by one of the participating employers in the fund, namely, Nedcor Limited, for 31 years. Prior to his retirement in July 1989 the complainant was head of Nedbank's International Banking Operations and a member of the Executive Committee. Although no other complainants have been joined in this matter, it is common cause that the complainant is actively supported in his complaint by four or five other pensioners. At all times prior to the lodging of the complaint, the complainant has spoken on behalf of the Nedcor Pensioners Association, of which he is the chairman. The Association has approximately 400 members. However, for reasons unknown, this complaint has not been brought in the name of the Association.

The respondent is a defined benefit fund duly registered under the Pension Funds Act of 1956 and in terms of its rules, has as its object the provision of benefits for employees and former employees of the employer on their retirement or, upon the death of such employees, for their dependants.

The fund is managed by a board of trustees which consists of fifty percent member-elected representatives, two of whom represent pensioner members of the fund.

As at 4th March 1998 the fund had a total of 8614 members made up as follows:

5200 in service members

3245 pensioners and dependants

169 deferred pensioners

With effect from 1st January 1994, two new retirement funds were established within the Nedcor Group of Companies. These were the "Nedcor Defined Contribution Provident Fund" and the "Nedcor Defined Contribution Pension Fund" (the "defined contribution funds"). At the same time, the Nedcor Pension Fund took a resolution not to admit additional members.

When the new funds were established, in-service members of the respondent were offered the opportunity to move to one of the defined contribution funds. The option to transfer from the respondent to either of the defined contribution funds was entirely voluntary. Subsequent to 1st January 1994, the members and erstwhile members of the respondent were given two opportunities to transfer to the defined contribution funds, the first on 28th February 1994 and the second on 1st January 1995. Since 1st January 1994, 4388 erstwhile members of the respondent have transferred to the defined contribution funds. At the time of transfer, the transfer arrangements provided that the transfer value in respect of each member transferring from the respondent to the defined contribution funds would be equal to the value of each individual member's past service actuarial reserve.

During the course of 1997 the board of the respondent decided to restructure the fund. After taking advice from various actuaries and consultants, the board of trustees convened a special meeting of the board on 13th October 1997. At that meeting a resolution accepting the restructuring proposal was adopted by the

trustees. The resolution enjoyed the support of both pensioner appointed trustees. The key elements of the restructure are as follows:

10 In-service members will be given a final option to transfer to the defined contribution fund with effect from the 1st January 1998. The member's transfer value will be his/her actuarial reserve value as at 31st December 1997 but assuming a 9 percent salary increase as at 1st January 1998. This amount will be enhanced by 18 percent to reflect the transfer of the investment risk to the member in a defined contribution fund.

20 The assets backing the pensioner's liabilities will be separated from the assets backing the in-service member liabilities by securing them via two with-profits pension policies from two insurance companies (Old Mutual - 70%; and Sanlam - 30%). However, prior to acquiring the policies, the pensions would be increased by an amount of 27% (representing 9% as the normal 1st January 1998 increase and an 18% enhancement to be consistent with the in-service members). In addition, individual pensioners will be given the right to apply to the board of trustees to have their pensions secured on a different basis. If the trustees approve such an application, the pension will be secured by way of a policy between the pensioner and the insurer. In other words, pensioners will be given the option to use their enhanced actuarial reserve to purchase the pensions of their choice from another registered insurer. In which event, the pensioner and his/her dependents would have no further claim against the respondent.

30 Former members of the respondent who during the course of 1994 and 1995 elected to transfer to the defined contribution fund, and who are still in the employ of Nedcor, or who have retired or died in the intervening period, will also receive an enhancement for the shift of the investment risk to the member by virtue of the transfer from a defined benefit scheme to a defined contribution scheme. This retrospective enhancement will be

18% of the members' actuarial reserve value at the time of transfer, together with 15% per annum interest from that date to 1st January 1998, or earlier retirement or death.

40 As a consequence of the restructuring, it was estimated that the respondent would be left with a market value surplus somewhere between R81 million and R141 million depending on the number of in-service members transferring to the defined contribution fund.

50 The financial position taking into account the different transfer scenarios was estimated by the actuaries Alexander Forbes on 4th November 1997 to be as follows:

NEDCOR PENSION FUND

ESTIMATE OF CURRENT POSITION

	All Actives Transfer Rmill	Half Actives Transfer Rmill	No Actives Transfer Rmill
Market Value of Assets	2.561	2.561	2.561
Less			
Cost of with profit annuities (= Estimated basic liabilities for pensioners and deferred pensioners plus 27% plus cost of CPI minimum = R913 mill x 1,27 + R10 mill)	1.170	1.170	1.170
Less			
18% enhancement to former active members (excluding resignations and retrenchments) (= R350 mill x 0,18 + interest at	110	110	110

15% p.a. compound)			
Less			
Transfer of actives with 18% enhancement + 9% extra to allow for 01.01.98 salary increase (= R898 mill x 1,27)	1140	570	-
Remaining market value	141	711	1.281
Less			
Liabilities in respect of remainder	-	490	980
Less			
Cost of future contribution shortfall	-	110	220
Market Value Surplus	141	111	81
	======	=======	=======

Given the likely existence of a surplus, the resolution of the trustees gave recognition to some entitlement on the employer's behalf to seek a reduction in its contributions to the respondent. Paragraph 1.7 of the resolution reads as follows:

> "The rules of the defined benefit pension fund provide that the actuary can recommend a reduction in the employer contribution if there is sufficient surplus in the fund. Even if the employer does take a contribution reduction, the employer continues to underwrite the benefits in terms of the rules of the fund"

Paragraph 7 of the resolution gives a fuller indication of the board of trustees' attitude towards an employer "contribution holiday". It makes the point that the rules of the defined benefit pension fund provide that the actuary can recommend a reduction in the employer contribution rate if there is sufficient surplus in the fund. However, it is noted that the employer does not wish to take a repatriation of the surplus, but simply wants to benefit from the surplus to the extent that it can take a contribution reduction. It is further noted that the law on the issue of who owns the surplus is somewhat unresolved and finally concludes that the

trustees would regard it as fair for the employer to benefit from 25% of the market value surplus. However, the trustees qualified this view in paragraph 7.4 of the resolution as follows:

> "Furthermore the employer will only benefit from the surplus if and to the extent that it is not required to underpin the benefits provided for in terms of the rules of the Nedcor Pension Fund, and the employer will continue to underwrite benefits (for e.g. in the event of failure of either of the insurers)."

The respondent maintains that the driving forces behind the restructuring proposals were the following:-

10 to provide a further option to members to transfer to the defined contributions funds;

20 the legislative changes enabling pensioners to buy pensions directly from insurers;

30 the need to "ringfence" and protect pensioners assets against taxation and an increasingly volatile investment market;

40 the changing employee remuneration environment, which requires full access to the employer contributions upon termination of service.

In response to these factors, the respondent appointed a task force to investigate the various options for restructuring. The task force came up with four options. These were:

10 The fund could retain the status quo.

20 The fund could split the assets into those required to underpin the liabilities to the pensioners and those required to underpin the liabilities to in-service members. The assets underpinning the liabilities to the pensioners could then be used to outsource the investment required to underpin their liabilities by means of purchasing an insurance policy which guaranteed the pension payments required, plus growth. The effect of such an option on the balance sheet would simply be to substitute insurance policies for equity and loan investments. Restructuring would not involve a termination of the fund's liabilities towards its pensioners. The pension benefits remain the obligation of the fund and the rules of the fund continue to apply. In other words, the employer would continue to underwrite the liability of the fund by virtue of its obligation to make periodical contributions in accordance with the rate determined by the valuator to meet the balance of cost as contemplated in rule 8 of the rules.

30 Thirdly, the trustees could have provided for an additional voluntary transfer to the defined contribution funds.

40 In addition to outsourcing the pensioners' liabilities, the trustees could have required a compulsory transfer of all active members to the defined contribution fund.

As has already been outlined, the trustees opted to outsource the pensioner's liabilities and to provide a further voluntary transfer of active members from the defined benefit fund to the defined contribution fund.

Research demonstrated to the trustees that the outsourcing would probably mean greater security for the pensioners and greater returns in that the pensioners would receive performance related benefits. From the figures available it appears that the chosen policies have out performed the annual

pension increases paid by the respondent for the past six years. This is evident in the table provided in the explanatory documentation distributed to the pensioners. It reveals the following:

Date of Increase	Nedcor Pension Fund Increase	Old Mutual & Sanlam combined % Increase
1st January 1993	13.0%	13.3%
1st January 1994	9.5%	10.9%
1st January 1995	8.75%	10.7%
1st January 1996	9.5%	9.6%
1st January 1997	7.5%	11.1%
1st January 1998	9.0%	11.8%

The important point to note about the transfer of the pensioner liabilities is that the respondent is not buying policies for each pensioner. The respondent is not transferring the actuarial reserve of each member to Old Mutual and Sanlam. The respondent remains liable for the defined benefit pensions and the employer continues to underwrite the fund's obligations. Moreover, no transfer of business to the insurers will take place in terms of section 14 of the Pension Funds Act 24 of 1956. The only section 14 application that is required in terms of the restructuring scheme is in respect of the transfer of in-service members and the additional enhancement payable in respect of former members.

The effect of the investment of the pensioners' liabilities with Old Mutual and Sanlam is that the two insurers will annually declare bonuses on the assets held in their portfolios, taking into account the returns achieved on these assets. The intention of the trustees is to add the declared bonuses as an annual increase to the pensions. As already indicated above, the bonuses of the insurers have consistently out performed the cost of living index and the pension increases previously offered by the respondent. Moreover, the respondent in its papers has conceded that should this in any year not be the case, nothing in the restructuring scheme or the rules precludes the trustees from granting an

increase or supplementary pension consistent with the consumer price index. Nevertheless, the board of trustees were confident that the investment in the insurance policies will generate benefits which match the fund's liabilities to and the reasonable benefit expectations of the pensioners. They believe the guarantee fund policies to be stable, reliable and secure investment vehicles, less subject to fluctuations in the market than the fund's current investments.

Subsequent to the decision to embark upon the restructuring, information was disseminated by the respondent to the pensioners in the fund and to the active members of the fund advising them of aspects of the scheme and the effect it was likely to have upon them. In addition, the scheme for the proposed transaction, in particular, those aspects of it involving a transfer of business from the respondent to the defined contribution funds, was submitted to the Registrar of Pension Funds for his approval in accordance with section 14 of the Pension Funds Act of 1956. The documentation in support of the submission was subject to alteration and change which unfortunately has resulted in some confusion in this dispute. I shall revert to this matter below.

After discussions with the Registrar's office, the respondent passed resolutions amending certain of the rules in order to give effect to the restructuring proposals. The resolution amending the rules of the fund has been submitted to the Registrar in accordance with section 12 of Act and are currently pending his decision. (The complainant originally made application to me to interdict the respondent from proceeding with these amendments. However, once it was evident that I was able to proceed with the main complaint prior to the Registrar taking a decision, the complainant withdrew his application for an interdict.) The content of the rule changes shall be discussed more fully below.

During 1995, the complainant and his group of associated pensioners, being fully aware of the worldwide trends in the pension industry to move from defined benefit arrangements to defined contribution arrangements, embarked on a process of negotiation to protect their interests. On 21st May 1996, a number of

pensioners, including the complainant, addressed a letter to the principal officer of the respondent. In the letter the pensioners make some significant observations and a number of legitimate requests for information. The pensioners seemed to accept that restructuring was an inevitable administrative consequence of the recent introduction of a tax on retirement fund rental and interest income accruing to the in-service members of the fund. For these reasons, they requested information on how the respondent intended restructuring and asked for an assurance that the pensions would be enhanced annually to compensate for inflation. They accordingly proposed an ongoing dialogue and requested certain documentation to be placed at their disposal.

The initial response of the fund to this offer of an ongoing dialogue was negative. In his letter of reply, the then principal officer of the fund claimed to be under no obligation to interact with the Association. In his view, the elected pensioner trustees were the representatives of the pensioners of the fund. Nevertheless, he did leave the door open for further negotiations. These negotiations endured over a period of some months until eventually in a letter dated 29th October 1997 the complainant broke them off.

As shall be seen more clearly presently, the complainant alleges that he was constrained in his negotiations with the respondent by the fact that he and the other members of the fund were not provided with adequate information regarding the proposed restructuring. He is of the view that the information given to the members was selective and "lacking in hard facts", particularly as regards the detailed financial implications for the fund and its members.

At various meetings between representatives of the Association and representatives of the respondent during October 1997, the Association put forward a contrary set of proposals for restructuring the fund. In summary these proposals proceeded on the basis that in terms of the rules of the fund (discussed more fully below) neither the employer nor the former members of the fund who had transferred to the defined contribution fund were entitled to share

in the market value surplus of the fund. The fund was obliged to give preference to the interests of the pensioners and the in-service members of the fund over those of the other two constituencies. Consequently, the pensioners argued, that the first priority of the trustees should have been to adjust the pensions upward to compensate fully for the increases in the consumer price index from the time of retirement. Prior to 1997 the policy of the respondent had been to hold annual upward adjustments of the pensions to approximately 80% of the increase in the consumer price index. The natural consequence of this policy was that older pensioners especially had experienced a decline in the purchasing power of their pensions. Thus, so they contended, an equitable distribution of the market value surplus should be accomplished by firstly making the upward adjustment to bring all pensions in line with the CPI from the time of retirement and then to grant pensioners an enhancement similar to that granted to the in-service members. Furthermore, it was proposed that the employer should bear the cost of the inducement to in-service members aimed at getting them to move from the defined benefit fund to the defined contribution fund. Finally, it was pointed out that there was no legal obligation on the part of the fund to include former in-service members who had transferred to the defined contribution funds in the enhancement exercise. Nevertheless, the Association indicated that it would not object to an enhancement being granted to former members provided this would not prejudice the pensioners in their efforts to obtain both the proposed adjustment and enhancement. Furthermore, the pensioners were adamant in their view that the employer had no claim whatsoever to any part of the market value surplus.

In response to these proposals the only concession the respondent was prepared to make was that if the proposed 1998 increase and the 18% enhancement of pensioner benefits did not compensate fully for the increase in the consumer price index from the time of retirement, the respondent would top up individual pensions to bring this about. The pensioners' reply to this was to argue that the allocation of part of the 18% enhancement to the cost of the overall consumer price index adjustment perpetuated a disparity between retired and active

members, in effect discriminating unfairly between them.

After further exchanges of information between the parties, as already mentioned,the parties reached a deadlock on 29th October 1997.

On 29th December 1997 the complainants' then attorneys of record addressed a letter of complaint to the principal officer of the respondent. It is common cause between the parties that this letter constitutes the "written complaint" which the complainant is required to lodge with the fund in terms of section 30A(1) of the Act before the Pension Funds Adjudicator acquires jurisdiction (section 30(A)(3)) to determine the dispute in terms of Chapter VA. The relevant part of the attorneys' letter of complaint reads as follows:

> **"We are accordingly instructed to notify you that our client will not be accepting the trustees proposals unless they are substantially amended and he reserves his right to challenge the decision of the trustees to restructure the fund and the basis of their proposals. His reasons for rejecting the proposals include:**
>
> **60 the direct or indirect allocation of part of the market value surplus to the employer, which is contrary to the rules of the fund;**
>
> **70 the direct or indirect allocation of part of the market value surplus as further benefits to former members who previously moved to other funds, or their dependants, which is contrary to the Pension Funds Act, 24 of 1956, and to the rules;**
>
> **80 the inequitable and arbitrary distribution of the surplus as between pensioner members and active members;**
>
> **90 the failure to give full recognition to the reasonable benefit expectations of pensioners and to comply with the established**

practice of the fund;

100 breaches of the rules and proposals which exceed the powers of the trustees;

110 the element of compulsion without an accompanying freedom of investment choice such as was afforded to active members in 1994 and subsequently.

These grounds of complaint, and the reasons for them have been raised in a detailed submission which our client has made to the Financial Services Board. Accordingly, we do not repeat them in this letter. Our client will await the outcome of the FSB's intervention before decided on what further steps to take in order to protect his rights."

The letters to the Financial Services Board referred to in the attorneys' letter are part of the complainant's bundle of documents and are marked annexures "W" and "X" and are dated 29th October 1997 and 4th December 1997 respectively.

Subsequent to lodging his complaint with the fund on 3rd January 1998, the complainant addressed another letter to the principal officer requesting information about whether the average returns on the Old Mutual and Sanlam policies were nett percentage increases or whether they were the gross amounts prior to the deduction of fees and administrative charges. He also requested to know what the guarantee fee charged by the two insurers would be and how this would be calculated and settled. The respondent replied to this letter on 9th January 1998 and included a letter from its actuaries and consultants responding to these two questions.

The respondent responded to the complainant's complaint on 14th January 1998. The complainant was not satisfied with the reply and instructed his attorneys to lodge a complaint with the Pension Funds Adjudicator in terms of section 30A(3)

of the Act.

On 3rd February 1998 the complainant's attorneys, lodged a complaint with the Pension Funds Adjudicator in terms of section 30A. In the conclusion of its letter of the 3rd February 1998, the complainant's attorneys reserved the rights of their client to supplement the complaint. A fuller complaint was lodged with the Adjudicator on 4th March 1998. In the interim there was an exchange of correspondence between the parties and the Financial Services Board regarding the registration of the amendments to the rules of the fund. As far as it is known, at the date of this determination, the amendments to the rules submitted by the respondent have yet to be approved by the Registrar.

The Complaint

Section 1 of the Pension Funds Act defines a complaint to mean:

> **"A complaint of a complainant relating to the administration of a fund, the investment of its funds or the interpretation and application of it rules, and alleging -**
>
> **10 that a decision of the fund or any person purportedly taken in terms of the rules was in excess of the powers of that fund or person, or an improper exercise of its powers;**
>
> **20 that the complainant has sustained or may sustain prejudice in consequence of the maladministration of the fund by the fund or any person, whether by act or omission;**
>
> **30 that a dispute of fact or law has arisen in relation to a fund between the fund or any person and the complainant; or**
>
> **40 that any employer that participates in a fund has not fulfilled its duties in terms of the rules of the fund.**

The complainant's complaint in this matter relates to the administration of the fund, the investment of its funds and the interpretation and application of its rules, and contends -

120 that certain decisions of the respondent were in excess of their powers under the rules of the fund, alternatively, an improper exercise of their powers;

130 that the complainant has sustained and will sustain prejudice in consequence of the maladministration of the fund by the respondent; and

140 that disputes of fact and law have arisen in relation to the fund between the complainant and the respondent.

Essentially, the complainant has made six complaints against the respondent.

It is proposed to deal with each complaint separately hereunder.

Complaint I - The disclosure of information

The complainant alleges that he is entitled to information from the respondent concerning his rights and benefits, which would enable him to assess whether the respondent's restructuring of the fund and the consequent distribution of the market value surplus is reasonable and equitable and accords full recognition to his rights and reasonable benefit expectations. He further alleges that the respondent has decided to withhold such information. The complainant's claim in this regard is based on the rights derived from section 7D(1)(c) of the Act which provides that amongst the duties of a board, the board shall -

"ensure that adequate and appropriate information is communicated to the

members of the fund informing them of their rights, benefits and duties in terms of the rules of the fund."

Furthermore, support for the existence of a duty to disclose information can be found in section 7C(2)(b) which obligates the board of a pension fund to act with good faith. The standard and extent of disclosure set by Section 7D(1)(c) requires the communication of *adequate and appropriate* information. The purpose of disclosure is to inform members of their rights, benefits and duties in terms of the rules of the fund. Accordingly, it would seem logical, just and equitable that the board should disclose such information as would reasonably enable the members to consider the consequences that the information held for them. *(See National Union of Metal Workers of South Africa v Metkor Industry (Pty) Ltd* (1990) 11 *ILJ* 1116 (IC) 1124A.)

The complainant, correctly in my view, contends that section 7D(1)(c) affords the complainant the right to be placed in a position to assess whether a proposed restructuring of the scheme is reasonable and equitable and accords full recognition to his rights and reasonable benefit expectations.

Section 7D basically codifies the common law fiduciary duties of trustees which include a duty to act in good faith. This section has yet to acquire statutory effect (see section 7E discussed below). However, for the purposes of this complaint I am prepared to accept that the common law duty to act in good faith obliges trustees to disclose adequate and appropriate information.

The information which the complainant alleges that he has not been provided is twofold. Firstly, he requests full and detailed information on the financial implications of the proposed scheme supported by a full and detailed report from the actuaries. Secondly, he requests full and detailed information on the "Opti-Plus and Bonus Pension products" of the insurers and the actuaries' report on

how these compare with alternative appropriate investment products from Old Mutual and Sanlam or from other insurers. Accordingly, the complainant seeks an order ordering the respondent to provide the complainant with such information.

Adv Du Plessis, on behalf of the respondent, made three points in relation to this complaint. Firstly, he submitted that the complainant's allegation that the respondent took a decision to withhold information from the complainant is without factual foundation. Secondly, he argued that the complainant was indeed provided with adequate and appropriate information. Thirdly, he took the point that the complainant in his written complaint lodged with the pension fund in terms of section 30A(1) did not make a complaint based on a lack of information. Accordingly, so he argued, the complainant has not complied with the requirements of section 30A before lodging his complaint with Pension Funds Adjudicator. Mr Du Plessis, however, stressed that the respondent did not wish to hide behind the jurisdictional point, and therefore chose to address the substance of the complaint.

The first issue to be decided under this complaint, therefore, is whether the respondent took a decision to withhold information from the complainant. The complainant alleges in his founding complaint that the respondent's decision to withhold information was an improper exercise of its powers. From the documentary evidence available to me, the only evidence which suggests that the respondent may have taken such a decision is that contained in the letter from the principal officer of the respondent to the Nedcor Pensioners Association dated 19th August 1996 annexed to the complainant's founding document as annexure "I". The letter is written in response to the Nedcor Pensioners Association's request for an ongoing dialogue concerning the restructuring of the fund. The relevant past of the letter reads as follows:

> **"As we see the position, the Nedcor Pension Fund is under no obligation to interact with or formally recognise the Association as representatives of**

> the pensioners. It is therefore not obliged to give the Association information that is given over and above that which is given to the public. The elected representatives (Messrs Westraat & Baas) are the formally recognised representatives of the pensioners.
>
> Unless you can provide us with good reason to alter our view, we suggest that you deal with the elected representatives of pensioners of the fund."

Although Mr Kennedy did not press the point with much vigour, it is this letter which perhaps has been construed as "the respondent's decision to withhold information from the complainant concerning his rights and benefits". Mr Du Plessis argued that the principal officer's reply cannot be construed as a decision on the part of the respondent not to furnish information to the complainant. He further submitted that the attitude of the principal officer was perfectly justified. Unless proof was provided that the Association represented a significant number of pensioners, there was no obligation to recognise the Association. In any event, the principal officer left the door open for the pensioners to convince him to the contrary and further events demonstrated that the respondent was in fact prepared and did enter into discussions with the Association. Thus, the decision not to recognise the Association, which in any event was not a decision to refuse information to the complainant, was withdrawn and information was indeed provided. Accordingly, there is no evidence to support the complainant's allegation that the respondent took a decision to withhold information from him.

The more important issue under this complaint is, whether the respondent did or did not provide adequate, appropriate information to the complainant. When the restructuring process first got under way, the respondent took the position, as is evident from the principal officer's letter of 19th August 1996, that the pensioner elected trustees would be the communication medium through which the pensioners would be expected to communicate. With effect from mid August 1997, once the restructuring scheme was formulated, the respondent adopted a different approach. Over a two month period, there was a significant exchange of

documentation between the respondent and the complainant as well as a number of meetings for the purpose of sharing information. In order to determine whether there has been adequate disclosure, it is necessary to set out the history of this interaction in some detail.

In early August 1997 the pensioner trustees addressed a letter to all pensioners. In the letter, written by Mr Johan Westraat, the trustees advise the pensioners that their representations to the fund have generally been taken into consideration with a positive attitude by the members of the board. They draw attention to the fact that important developments were taking place but that it had been impossible to keep the pensioners fully informed because prior to then there had been no concrete decisions taken by the board in relation to the restructuring. The letter ends with an invitation to members to keep in contact with the trustees regarding the restructuring exercise.
On 9th August 1997, the complainant addressed a letter to the principal officer of the respondent in which he advises that he has recently become aware of a plan to give pensioners the option to withdraw from the fund. He goes on to express concern and the hope that the Pensioners Association would be given early insight into the plans and that they would be provided with sufficient information. In his response, dated 18th August 1997, the principal officer notes the complainant's concern over the lack of information on the granting of options to pensioners to withdraw from the fund. He mentions, however, that the whole question of the future of the fund was under discussion and that the pensioner representatives were both being kept fully in the picture and had so far participated actively in the negotiations. This response was consistent with the respondent's view that the pensioner trustees were the appropriate representatives of the pensioners.

Once the restructuring scheme was formulated, the respondent agreed to meet with the Pensioners Association representatives and entered into correspondence with them. The fact that prior to this the Nedcor Pensioners Association had been sidelined was a matter of some frustration to the

complainant and his associates. On 29th September 1997 the complainant addressed a letter to the chairman of Nedcor Ltd, Mr C F Liebenberg, in which he makes a complaint about the failure of the fund to provide him with sufficient information. Although not clear from the evidence, perhaps this letter led to a change in attitude. On the next day the complainant telephoned the principal officer of the fund and requested certain documents. These documents included the fund rules, details of the proposed scheme, actuarial reports, financial results, etc. These were couriered to certain members of the Association, including the complainant.

On 3rd October 1997, the complainant acknowledged receipt of the documents and requested additional information. The complainant asked for four specific items of information, viz:-

15. the actuaries' detailed recommendations as to how they proposed calculating the improved or enhanced benefits of pensioners as well as the transfer of values of the various groups that would be affected by the restructuring;

16. the cost to the fund of implementing the proposals and the impact this would have on the market value surplus;

17. the cost to the fund of providing for early retirement and retrenchment packages and revised vesting scales and the impact this would have on the market value surplus;

18. the detailed basis on which the fund intended transferring the pensioners' liabilities into smooth bonus portfolios, inter alia the rate of interest assumed in the calculations.

The principal officer replied to the letter on 3rd October 1997 indicating that the matter had been referred to the actuaries and undertook to revert to the

complainant once he had additional information. Two subsequent letters (annexures "M" and "N" to the complainant's complaint) written by the principal officer and a consultant actuary, both dated 7th October 1997, deal with the issues raised in the complainant's letter of 3rd October 1997. Although the actuary queries the relevance of some of the information in his reply, it is evident from the letter that he attempts to the best of his ability to address the issues raised.

Two days later on 9th October 1997 the respondent met with three members of the Association including the complainant and their actuarial advisor, Mr Maxwell, of the firm Ginsberg Malan. This meeting was followed by a letter written by the complainant dated 11th October 1997 (annexure "Q" to the complainant's complaint). Attached to the letter is a summary of the issues debated at the meeting which indicates that the entire restructuring scheme was discussed in some detail.

The second paragraph of the letter is revealing. It reads:

> "We greatly appreciate the time you and your colleagues set aside for us especially at this busy financial year end period. We gained immensely from hearing for the first time in detail, of the reasoning behind and the motivation for the proposals affecting our fund and its members. If ever it was true that by listening to the other party's point of view much understanding is gained, this was it. I sincerely hope that the feeling was mutual."

The complainant goes on to express his pleasure that the Association has been invited to help with the vetting of the circular explaining the restructuring to the pensioners. In this regard he observes:

> "It was pleasing to note your shared feeling that the fund's advices should be frank, open, plain and scrupulously honest."

He then proceeds to make certain suggestions concerning the draft circular.

In the annexure to the letter of 11th October 1997, essentially being a minute of the meeting of the 9th October 1997, the complainant traverses the various issues arising as a consequence of the restructuring. At no point in the document does he complain about the failure to disclose information.

On 15th October 1997 a meeting was held between the principal officer of the respondent, one of the trustees representing the pensioners (J C Westraat) and two representatives of the Nedcor Pensioners Association (the complainant and Mr A van der Merwe-Vance). The purpose of the meeting was to report back on the meeting of the board of trustees held on 13th October 1997 at which the issues raised at the meeting of 9th October 1997 were discussed. The complainant subsequently prepared a summary of the issues debated at that meeting, effectively amounting to a minute of the meeting. Various issues concerning the restructuring are dealt with. Amongst other things, it was pointed out to the Pensioners Association that the fund had hedged the market value surplus and that this introduced an element of urgency requiring the exercise to be proceeded with. Nowhere in this minute is there any complaint that information required had not been disclosed.

In response to the various concerns raised in the correspondence and in the meetings held between the respondent and the Pensioners Association, the board instructed their attorneys to respond in writing to certain criticisms and reservations expressed by the Association in its memorandum attached to the letter of 11th October 1997. The letter concentrates primarily on two areas of the restructuring proposals, namely:

19. the right of the employer to benefit in any way from the market value surplus; and

20. the allocation of a portion of the surplus to the former members of the respondent who had transferred to the defined benefit

contribution fund since 1994.

In effect, the letter is a full and comprehensive exposition of the respondent's position in relation to these two issues. Relying on the decision in *Lorentz vs Tek Corporation Provident Fund and Others* 1998 (1) SA 192 (W), the opinion concludes that the employer is entitled to some benefit from the market value surplus. Regarding the enhancement for former members, the attorneys argue that because the advice at the time was that the employer was entitled to the benefit of the full amount of the surplus, the former members had been transferred without any benefit of the surplus, and that, therefore, in equity they were entitled to have the benefit of the surplus retrospectively. In their view, the equity of the proposal was beyond question, yet they recommended an amendment to the rules to ensure that the proposal was effected in accordance with law.

On the same day, 22nd October 1997, a further meeting was held between the respondent and the Association at which the respondent's actuarial advisor took the representatives of the Association through the issues the trustees had considered when arriving at the restructuring proposals. The minute of this meeting (annexure "T") reveals that the respondent's attorneys' opinion was fully discussed and that the principal point of dispute in that regard was whether or not the surplus was partly as a result of an over contribution by the employer in the past. The Association took the view that there was no evidence in the actuarial report to support a claim of entitlement to share in the surplus. In the conclusion of the minute, the complainant records the following:

> **"Actuarial report will also be submitted. We are to be given sight of this as well as detailed information on the proposed investment in Opti-Plus."**

On 24th October 1997 the principal officer of the respondent furnished the complainant with a copy of a six page report prepared by Mr Gary Scott, an actuary at Old Mutual Actuaries and Consultants. (Annexure "U"). The document

indicates that three insurers (Liberty Life; Old Mutual; and Sanlam) were approached to tender for the provision of with-profits annuities to the pensioners of the Nedcor Pension Fund. The document then compares the three tenders and furnishes an assessment of the tenders. The total consideration for the tender is in the region of more than R850 million. Apparently, Old Mutual and Sanlam are the only insurers who have experience in managing a portfolio of such a size. Accordingly, the actuarial report recommends that if the board decided to appoint two insurers, Old Mutual and Sanlam should be chosen. However, if only one insurer was to be selected, the actuary recommended that Old Mutual be chosen on account of its higher asset cover and larger size.

The actuarial report provides no information explaining the source of the market value surplus or setting out the extent to which it derives from employer over-contribution. The only evidence presented in these proceedings explaining the source of the surplus is contained in annexures "R15" and "R16" to the respondent's reply which was furnished to the complainant only on 10th March 1998 as part of the documentation for the hearing of this complaint. As shall be seen, these documents claim that the employer is entitled to share in at least R300 million of the surplus, but offer little substantiation of that claim.

A few days later, on 29th October 1997, the complainant in his capacity as chairman of the Nedcor Pensioners Association, addressed a letter to the principal officer of respondent. In this letter, he complains about the respondent's reluctance to debate the issues or to negotiate in an attempt to find common ground and arrive at a consensual set of proposals. He records that the parties are at impasse and declares that in the light of that impasse the Association has decided against making further representations to the board. He informs the fund of the intention of a number of members of the Association to petition the Pension Funds Adjudicator collectively on the issues the Association has espoused. Significantly, in setting out this decision to cut off negotiations, the complainant makes no reference to a lack of information. It is more than apparent that the basis of the breakdown in the relationship is the absence of

consensus.

On the same day, the complainant addressed a letter to Mr Andre Swanepoel, the Registrar of Pension Funds, concerning the restructuring of respondent. In it he complains about the ongoing reluctance on the part of the board of trustees to debate the issues or to negotiate them in an attempt to find common ground and arrive at a consensual set of proposals. Again he makes no complaint about the failure of the fund to disclose information. In a letter addressed to the head of the actuarial department of the Financial Services Board dated 4th December 1997 (annexure "X") the complainant once more complains about the failure of the respondent to engage in negotiations and provides a detailed memorandum setting out all of the issues and questions in dispute. Yet, nowhere in the letter or the twenty page memorandum does the complainant make the complaint that he has been denied adequate and appropriate information.

Finally, in his formal letter of complaint in terms of section 30A(1), addressed on his behalf by his attorneys, the complainant also makes no complaint about a lack of information.
As already mentioned above, subsequent to lodging his formal complaint, the complainant did request additional information (annexure "Z") concerning the percentages and the guarantee fee. On 9th January 1997 the respondent replied to these queries by including a report of the actuary, Mr Scott. The complainant did not respond to Mr Scott's reply to his query, nor prior to the hearing of this matter, was it alleged that the information provided was in any way insufficient or inadequate.

No further requests for information or complaint about the disclosure of information was made by the complainant until it formally lodged its complaint with the Pension Funds Adjudicator in terms of Section 30A(3) of the Act.

The respondent argues that in the light of this history of correspondence and meetings, the fund has discharged its obligation to disclose adequate and

appropriate information. Indeed, the evidence seems to suggest that with one exception, after 11th October 1997 (see annexure "Q") when the complainant expressed his gratitude for being furnished with information, the complainant had no further complaint about the disclosure of information until the lodging of his complaint with the Pension Funds Adjudicator. The exception is the request for a report on the source of the surplus and the extent to which the employer over-contribution accounts for it.

As stated, the complainant has requested an order for "full and detailed information on the financial implications of the proposed scheme supported by a full and detailed report on the actuaries". When Mr Kennedy was pressed during the hearing to be more specific about the information the complainant still required, he essentially asked for three pieces of information, namely:-

21. an actuarial report on the implications of outsourcing the pensioners liabilities;

22. information on the fee paid to the insurers; and

23. a comparative assessment of the various pension products and alternative appropriate investment products for outsourcing the pensioners' liabilities from Old Mutual and Sanlam and other insurers.

It is the respondent's submission that the two reports submitted by Mr Gary Scott dated 24th October 1997 (annexure "U") and 6th January 1998 (annexure "AA") respectively furnish this information. Mr Scott's report of 24th October 1997 indicates that the total consideration for outsourcing the pensioner liabilities was between R855 million and R864 million. All three insurers' prices compare favourably with the actuarial estimate of the fund's basic liabilities for the pensioners, being R1.17 billion. In his letter of 6th January 1998 (annexure "AA") Mr Scott makes it clear that all fees levied by Old Mutual and Sanlam were included in the calculation of the initial purchase price and that no further fees

would be payable. He concedes, however, that the insurers may include an explicit allowance for the fact that the pensions and other increases are guaranteed. Often this allowance is incorporated in the other assumptions used in the calculation of the purchase price. Essentially, therefore, it would seem that the information which the complainant requests in this respect has already been supplied.

Mr Kennedy made some argument that the comparative assessment should go further than the three insurers consulted. The respondent countered that it would be pointless to order a comparative assessment by other insurers where there are no other insurers in the market place that have experience in handling a portfolio of more than R800 milliion.

Even were I to accept that the complainant should have the benefit of a fuller comparative assessment, the consequence of my making such an order would be to suspend these proceedings pending the completion of the assessment and thereafter a reconvening of the proceedings to entertain further evidence and submissions in relation to it. In essence, the complainant is seeking an interlocutory interdict, which I am permitted to grant in terms of my powers under section 30E of the Act. Before granting such an interdict, however, a presiding officer should have regard to the balance of convenience. As already discussed, the complainant has not sought such a comparative assessment prior to lodging his complaint in terms of section 30A(3) of the Act. The belated raising of this complaint, and particularly the relief claimed by the complainant in this regard, will prejudice the respondent because of the further delay in implementing the scheme which will necessarily follow the granting of such relief. It is common cause that the respondent has arranged for the assets of the fund to be hedged against fluctuations in their value due to market fluctuations, and the fund has consequently been spared the significant depreciation in the market value of the underlying assets since the hedge was put in place. The hedge on the assets expires on 15th April 1998, on which date the fund will receive its investments at then market value together with the cash difference between the market value of

the underlying assets at the time when the hedge was put in place and the market value of the underlying assets on 15th April 1998. Thereafter, however, the underlying assets will be subject to the vagaries of the market. The valuator has certified that the restructuring proposals are financially viable and acceptable on the basis of the hedging exercise. The viability of the proposals could significantly change once the hedge expires. Should the hedge be allowed to expire by virtue of the relief sought by the complainant being granted, the restructuring proposals as a whole will become unviable. The pensioners of respondent also have been receiving the 27% enhancement since January 1998 in anticipation of the restructuring proceedings. In the absence of implementation it will be difficult to restructure the pensioners' liabilities.

Accordingly, in my view the balance of convenience favours the respondent. The negative implications of the hedge expiring far outweigh the benefit the pensioners may derive from a further comparative assessment of investment products, if indeed that is at all possible. In my view, the pensioners had sufficient information at their disposal to seek further advice from other insurers should they have wished to do so. Some of the pensioners in the Pensioners Association are former senior executives in the banking industry, and they would have had access to financial expertise and advice on the comparative benefits of different products beyond those presented by the respondent.

Accordingly, I am satisfied that the reports of the actuaries contained an annexure "U" and annexure "AA" presented by Old Mutual Actuaries and Consultants provide sufficient information on the outsourcing of pensioner liabilities to enable them to take further steps to protect their rights and interests. This is particularly so against the background of the various meetings and correspondence that preceded these reports. On these grounds and for the aforegoing reasons this part of Complaint I relating to the disclosure of information is dismissed.

However, I remain unconvinced that the complainant has been furnished with

appropriate and adequate information about the source of the market value surplus and the extent to which its existence derives from the over-contribution by the employer. The reports contained in "R15" and "R17" are hardly *adequate*.

Unfortunately for the complainant I am precluded on jurisdictional grounds from ordering the respondent to furnish such an actuarial report.

There is merit in the respondent's contention that the complainant has not complied with the requirements of section 30A before lodging the complaint with the Pension Funds Adjudicator. Prior lodging of a complaint with the fund or the participating employer is a jurisdictional prerequisite for the valid lodging of a complaint with the Adjudicator. The provision has a threefold purpose. Firstly, it affords the fund or the employer an opportunity to deal with the complaint without having first to justify its actions before the Adjudicator. Secondly, it gets the fund or the employer to formulate a reply narrowing the issues in dispute. As such, it establishes an alternative and an informal set of pleadings. Thirdly, it hopefully will prompt the industry to establish internal complaints procedures and mechanisms of compliance. Accordingly, it is essential that complainants comply with its terms.

The complainant lodged his complaint with the respondent by means of a letter addressed by his attorneys to the respondent dated 29th December 1997 (annexure "Y"). As already discussed, that letter did not contain a complaint based on lack of information.

The complainant has argued that I ought not to look at the dispute too technically, seeing that the issues raised clearly flow from the dispute as a whole. In other words, a holistic approach is called for in which each complaint should be seen as ancillary to the overall dispute.

Mr Du Plessis, for the respondent, conceded that there was much merit in such an approach generally. However, he argued that the holistic approach would not

be justified in the circumstances of this case. First of all, the dispute concerning the disclosure of information appeared to the respondent to have been settled by the end of October 1997 after the series of meetings that took place during the course of that month. Additionally, the written complaint lodged with the fund on 29th December 1997 does not treat the dispute in a holistic manner. Specific issues are referred to and are delineated in the letter. In such circumstances the failure to raise a dispute about disclosure of information seems to suggest that at the time of lodging the written complaint there was no such complaint concerning disclosure. This means that the respondent has been denied its statutory right to deal with the complaint before the adjudication of it.

Accordingly, I find that the complainant has not lodged a complaint based on lack of information. And even though I am of the opinion that the respondent has failed to furnish adequate information on the source of the market value surplus, I lack jurisdiction to make an order compelling it to do so.

Be that as it may, as this information will be of ongoing value and relevance to the complainant, I strongly recommend that a full and detailed actuarial report analysing the source of the surplus and the extent to which it derives from the employer over-contribution be furnished to the complainant. Should the respondent fail to do so expeditiously the complainant may re-approach this tribunal for appropriate relief.

Since this information is relevant only to the employer's entitlement to share in the surplus remaining in the fund after the transfers - see discussion under Complaint III below - the failure of the respondent to furnish it in any event would not of itself justify suspending the operation of the restructuring proposals.

Accordingly, Complaint I is dismissed.

Complaint II - The *ex post facto* enhancement to former members

The complainant's second complaint relates to the elements of the restructuring benefiting the former members of respondent who elected to transfer to the defined contribution funds during 1994 and 1995. This aspect of the restructuring scheme is set out in paragraph (c) of the documents submitted to the Registrar of Pensions seeking an authorisation of the transfer of business in terms of section 14 of the Act. The said paragraph (c) reads:

> **The purpose of the scheme is ..... to provide for the transfer of additional amounts from the Nedcor Pension Fund to the Nedcor Defined Contribution Pension Fund and the Nedcor Defined Contribution Provident Fund in respect of former members of the Nedcor Pension Fund who transferred to the Nedcor Defined Contribution Pension Fund or the Nedcor Defined Contribution Provident Fund, on either 28th February 1994 or 1st January 1995, and who are still members of one of those funds or who have subsequently retired or died while a member of one of those funds.**

The resolution of the trustees on 13th October 1997 motivates this additional payment as "an enhancement for the shift of investment risk to the member in a defined contribution fund". The enhancement will be 18%, but only of the members retrospective actuarial reserve value at the time of transfer, together with 15% per annum interest from that date to the 1st January 1998 or earlier retirement or death.

The principal stated aim of this aspect of the restructuring was to ensure that earlier transferees received the same treatment as transferees who would transfer in accordance with the restructuring exercise during 1998. The 1998 transfer basis represents a change in the transfer basis when compared to the earlier transfers. The trustees felt that members who transferred earlier should not prejudiced by their earlier election. The trustees accepted that from a labour relations point of view this approach would be fairer and result in all employees of the participating employer being treated equally. In terms of clause 6.2 of the

resolution it was decided not to extend the retrospective enhancement to former members who had left the service of their employer as a result of retrenchment or resignation. The reasons advanced for this were as follows:

1. **preference should be given to those who are still part of the Nedcor family;**

2. **such ex-members have no legitimate expectations of an enhancement;**

3. **in the case of retrenchments, exit terms are negotiated between employee and employer, and not the fund;**

4. **it may not be possible to trace or pay all such ex-members, e.g. emigrants; and**

5. **no enhancements are being distributed to members who were retrenched or resigned prior to 1994.**

The complainant has consistently objected to the former members of the fund gaining substantially from the restructuring proposals. It is estimated that about R110 million of the market surplus will be distributed to the former members. The complainant argues that a decision to allocate a portion of the market value surplus to persons who are not members of the fund is:

6. **in excess of the powers of the fund in terms of the rules of the fund, alternatively an improper exercise of their powers;**

7. **a breach of the duties imposed by the Act;**

8. **a breach of the fiduciary duties of the trustees; and**

9. **amounts to maladministration of the fund.**

In support of his arguments the complainant relies on rule 17 *bis* and section 7C(2)(a) and section 14 of the Act.

Rule 17 *bis* is headed *"Transfer to another pension or provident fund of the employer"*. The content of the rule is as follows:

> **If the principal employer decides to establish another pension or provident fund for certain categories of employees, then all employees who at the time of the establishment of another pension or provident fund, are in such categories and are members of the fund shall have the option to elect whether they wish to become members of such other fund.**
>
> **Such election shall be made in writing within the option period agreed to by the trustees and shall thereafter be irrevocable.**
>
> **In this event the employees' membership of the fund shall cease and the employees past service actuarial reserve in the fund as determined by the valuator shall after payment of any income tax due and payable thereon, be transferred to such pension or provident in accordance with rule 15, rule 16 or rule 17.**
>
> **Thereafter the member shall not be entitled to any further benefit from the fund.**
>
> **Notwithstanding anything to the contrary contained in these rules, a portion of the benefits payable in terms of this rule 17 *bis* that represents the benefit the member would have been entitled to take in cash on his leaving service, shall be the member's own contributions (as defined in rule 36.1.9).**

On 6th February 1998 the trustees passed a resolution to effect two amendments

to rule 17 *bis*. These amendments have yet to be approved by the Registrar. The third paragraph of the rule is replaced by the following:-

> **In this event the employees' membership of the fund shall cease and the employees' past service actuarial reserve in the fund as determined by the valuator, together with such enhancements arising from any surplus in the fund as may be determined by the valuator as being in excess of the funding requirements of the fund and approved by the trustees in their sole discretion shall, after any income tax due and payable thereon, be transferred to such pension or provident fund; provided that a portion of the transfer value not exceeding a member's withdrawal benefit may at the member's option be transferred to a retirement annuity fund or, subject to the prior approval by the Registrar to a preservation vehicle.**

The fourth paragraph of rule 17 *bis* will be replaced by the following:-

> **Thereafter the member shall not be entitled to any further benefit from the fund; provided that the trustees shall, with the prior written approval of the principal employer be entitled in their discretion to allocate and transfer for the benefit of any such member (or former member who has previously elected to become a member of such other fund) such proportion of any surplus in the fund as determined by the valuator to be available for distribution, as the trustees may in their absolute discretion determine provided that such former member is an active or retired member of such other fund or the eligible spouse or dependent of such former member who at the time of his death or retirement was an active or retired member of such other fund.**

Additionally, the amendment inserts a fifth paragraph to rule 17 *bis*, which will read as follows:-

> **Any such transfer contemplated in rule 17 *bis* is subject to the issue by the**

Registrar of a certificate or certificates contemplated in section 14(1)(e) of the Act.

Throughout the negotiations between the fund and the Association, the complainant argued that in terms of rule 17 *bis* (as unamended) there is no obligation on the part of the fund to include former members in the enhancement exercise. Nevertheless, the Association has stated that it would not object if an enhancement was granted to former members in the interests of equity, provided there was no legal impediment to doing so and it was done subsequent to the adjustment of all pensions upwards to compensate fully for the increases in the consumer price index from the time of retirement, which exercise should occur prior to the 27% enhancement of pensions.

Additionally, it was contended that the trustees are obliged in terms of section 7C(2)(a) to take all reasonable steps to ensure that the interests of *members* in terms of the rules of the fund and the provisions of the Act are protected at all times especially in the event of an amalgamation or transfer of any business contemplated in section 14. Moreover the trustees are further required to act with due care, diligence and good faith and to act with impartiality in respect of all *members* and beneficiaries of the fund (section 7C(2)(b)(d)). The decision to transfer a share of the market value surplus to former members who transferred to the defined contribution funds, according to the complainant, does not protect the interests of *members* of the fund. Such a transfer, so he claims, is not reasonable and equitable and does not accord full recognition to his rights and reasonable benefit expectations.

The respondent seeks to justify the enhancement to former members on the grounds that at the time they were transferred it was of the mistaken opinion that the market value surplus belonged exclusively to the employer. When the former members transferred to the defined contribution funds there was a market value surplus in the fund and an 18% enhancement could then have been given. Notwithstanding this, those members who transferred only received their past

service actuarial reserve calculated without taking the surplus into account. Transferring members accepted this position.

The present restructuring exercise commenced at about the time the High Court handed down the decision in *Lorentz v Tek Corporation Provident Fund & Others* 1998 (1) SA 192 (W). This decision holds that the participating employer does not have an exclusive entitlement to the surplus and that the trustees are obliged to distribute the surplus in accordance with their fiduciary duties taking into account the interests of the members as well as those of the participating employer. In deciding to grant the enhancement to former members, the trustees were concerned to ensure fairness and no discrimination between members who transferred to the defined contribution funds at different times. It is further argued that the 1998 restructuring proposals constitute a continuation of the restructuring process which commenced in 1994. On this basis, the enhancements should have accrued to the former members and would have been received by them had the same approach been adopted then as has been done on this occasion.

The crisp issue for decision in respect of this complaint is whether the law or the rules of the fund prohibit enhancing the transfer of values of the former members.

Unfortunately, neither counsel for the complainant nor the respondent addressed me on the statutory or common law powers and duties of the trustees of a pension fund. This is to be regretted, especially since the complainant alleges that the enhancement to former members is in breach of those duties. Reference has already been made to section 7C and the codification of the common law fiduciary duties brought about by Section 7C(2). However, in terms of section 7E of the Act, section 7C (inserted by section 2 of Act No. 22 of 1996) only applies in respect of existing pension funds with effect from 15th December 1998 and in respect of funds registered after the amendment on or after 19th April 1997. The evidence shows that the respondent was registered before the amendment and therefore the provisions of section 7C shall only apply to it with effect from 15th

December 1998.

Be that as it may, the *Tek* Judgment has held that trustees are obliged to conduct the affairs of a pension fund in accordance with the common law regarding the fiduciary duties of those who occupy positions of trust in the wide sense. Moreover, section 2 of the Financial Institutions (Investment of Funds) Act 39 of 1984 applies to pension funds. Section 2(a) imposes a duty on the managers of a fund to observe the utmost good faith and to exercise proper care and diligence in the safe custody, control or administration of the funds. Section 2(c) further provides that those in control of the fund shall not alienate trust property of funds in a manner calculated to gain directly or indirectly any improper advantage for themselves or any other person at the expense of the institution, trust, beneficiary or principal concerned.

These statutory duties must be read in conjunction with the fiduciary duties imposed by the common law on those occupying positions of trust. *Honore: South African Law of Trusts* (214) usefully summarises the three main principles governing the administration of a trust. These are:-

10. the trustee must give effect to the trust instrument so far as it is lawful and effective under the law of the place where the administration has to take place;

11. the trustee must in the performance of duties and the exercise over powers as a trustee act with care, diligence and skill which can reasonably expected from a person who manages the affairs of another; and

12. except as regards questions of law the trustee is bound to exercise an independent discretion.

From these provisions, it would seem that the issue here crystallises to the

following question: Do the rules of the fund authorise the enhancement intended to be paid to former members? And would such a payment be contrary to the statutory duty of the trustees to observe the utmost good faith, to exercise proper care and diligence and not to alienate funds or trust property in a manner calculated to gain directly or indirectly any improper advantage for any other person at the expense of the fund or its members.

Clause 2 of the preamble to the rules of the fund defines the object of the fund as follows:

> **The object of the fund will be to provide benefits for *employees and former employees* of the employer on their retirement or upon the death of such employees, for their dependants. (emphasis supplied)**

The distribution of part of the market value surplus of the fund to former members of the fund who remain employees of the employer would therefore seem to be consistent with the object of the fund. Significant in this regard is the absence of any requirement that the fund should only benefit *members* of the fund.

Turning now to rule 17 *bis* (cited fully above) which regulates transfers between the various pension funds in which the employer is a participating employer. The purpose of this rule is to allow the employer to set up a variety of retirement funding vehicles with a view to spreading its risk across a range of options.

The complainant has relied principally on the third and fourth paragraphs of this rule, in its unamended form, to suggest that once the transfer is complete the fund is not permitted to offer further benefits or enhancements to the transferring employees.

Counsel for the complainant has submitted that to recognise any liability to anyone other than the retired and in-service members of the fund would entail a

reduction in a member's actuarially established interests. The argument presupposes that beyond the member's entitlement to a defined benefit, the member has some interest in the surplus of the fund. This may indeed be so. However, the counter argument is that the former members who transferred during 1994 and 1995 on the mistaken supposition that they had no rights or expectations to share in the surplus, have a renewed expectation to share in the surplus by virtue of the *Tek* judgment.

The fourth paragraph of the unamended rule 17 *bis* does not pose a bar to the trustees in meeting that renewed expectation of the former members of the fund. The rule simply provides that such former members will have *no right* to any further *benefit* from the fund. As such, that is no limitation on the discretion of the trustees to give effect to the object the fund which includes providing retirement benefits for employees and former employees of the employer. Moreover, the term *benefit* usually refers to the defined benefits guaranteed by the fund, namely: retirement benefits, withdrawal benefits, death benefits and disability benefits. A *benefit*, therefore, falls to be distinguished from a *transfer value*. The former members are not receiving further *benefits*, they are receiving *enhanced transfer values*.

Nor can the trustees decision to give the former members the benefit of the *Tek* ruling be considered to be an alienation of the funds property in a manner calculated to gain any improper advantage as contemplated in section 2(c) of the Financial Institutions (Investment of Funds) Act 39 of 1984. While it is certainly true that former members will be advantaged by the trustees, in light of the mistaken supposition, the continuing employment relationship between the employer and the former members, and the general precepts of fairness, such advantage can hardly be described as improper. Likewise, the decision to treat the former members equitably cannot be regarded as being *mala fides,* nor does it amount to maladministration. It is true that the legitimate interest of the pensioners in the surplus has been diminished by the decision to benefit the former employees. But, it needs to be emphasised that the pensioners' interest in

the surplus remains an expectation rather than a right. In an ongoing fund the pensioners have no right to partake of the surplus, they have only a right to a defined benefit. By the same token, as already mentioned, the former employees who transferred on the basis of mistaken supposition concerning their entitlement to participate in the surplus, equally have a legitimate expectation to share in the surplus, especially in the fuller context of what is in effect an ongoing restructuring of the various funds in which the employer is a participating employer.

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.

What is more, an analysis of the *Tek* decision (at p.233 -234) reveals that Navsa J in that case ordered the trustees of the pension fund to do precisely what the trustees in the present matter have resolved to do, namely to grant an *ex post facto* enhancement of a transfer value which was originally incorrectly limited to the actuarial reserve under influence of the mistaken supposition that the employer had exclusive entitlement to the surplus.

The complainant also places some reliance on the provisions of section 14 of the

Act. In particular section 14(1)(c) provides that the transfer of any business from a registered fund to any other person will not be of any force or effect unless the Registrar is satisfied that the scheme is reasonable and equitable and accords full recognition to the rights and reasonable benefit expectations of the persons concerned in terms of the rules of a fund concerned; and to any additional benefits the payment of which have become established practice. If the Registrar is so satisfied he is then entitled to issue a certificate to the effect that all the requirements for the transfer have been satisfied. The argument of the complainant is that at the time the former members transferred to the defined contribution funds such transfers received the sanction of the Registrar under section 14. The Registrar was satisfied that the transfer was reasonable and equitable and accorded full recognition to the rights and reasonable benefit expectations of the members of the fund. The former members transferred to the defined contribution funds entirely voluntarily and accepted the terms of the transfer. In other words, when the former members accepted the transfer out of the defined benefit fund, they accepted their transfer, the valuator's determination of their actuarial values and the Registrar's certification that the scheme was reasonable and equitable and accorded full recognition to their rights and reasonable benefit expectations. Had they been dissatisfied with the terms of the transfer they ought to have sought appropriate relief, but they did not do so.

The argument misses the very important point that at the time of the transfer, the former members, the trustees, the valuator and the Registrar were labouring under the mistaken supposition that the employer had exclusive entitlement to the surplus.

Moreover, no argument has been advanced that the section 14 certificates imposes a bar on the trustees exercising their discretion to benefit the former members as they have done in terms of their resolution of 13th October 1997. Section 14 does not say that the Registrar's certificate is the final determination of the effect of the transfer of business. It simply provides that no transfer shall be of any force or effect unless such certificate is granted.

In the *Tek* Judgment, Navsa J was faced with a similar argument. At 223A-C he dealt with the matter thus:

> **"It is apparent from the bundle of trial documents that the Registrar did not, when he/she approved the contribution holidays in this case, consider the questions discussed in this judgment relating to entitlements to surpluses. It is clear from (the) evidence that the prevailing view in the pension industry is that the surplus is available to the employer to use to take a contribution holiday. The Registrar, in approving this scheme involving the transfer of members to the provident fund, was content to do so even though the surplus was not applied to benefit the members of the pension fund. It is clear that the source of the surplus was not of concern to the Registrar, the trustees and Tek. In these circumstances, it can hardly be contended that the Registrar's certificate is conclusive."**

Finally, the complainant argues that the decision to benefit the former members is discriminatory in nature and effect in that it excludes former members of the fund who subsequent to transfer have been retrenched or who have resigned. The trustees resolution of the 13th October 1997 (paragraph 6.2) seeks to offer some justification for this differential treatment. Essentially, the trustees feel obliged to grant equal treatment only to those who are still part of the Nedcor family. Besides, the respondent argues, the complainant cannot take up the cudgels on behalf of the retrenchees or those who have resigned. The complainant counters that what is fair and reasonable has to be assessed as a single exercise taking into account all relevant parties and considerations.

There is no evidence before me of the number of former members who have resigned or who have been retrenched since the restructuring exercises of 1994 and 1995. Hence, it is difficult for me to make a ruling on whether their differential treatment is unjustifiable to the extent that it renders the trustees decision an abuse or improper exercise of power. Even were I to conclude that the exclusion of the early withdrawals was discriminatory, it is questionable whether such discrimination should lead to the setting aside of the trustees'

decision. Had such former members been joined as complainants in this matter, and were they to persuade me that the differential treatment of the early withdrawals did constitute unfair discrimination, I daresay I would have used my powers under section 30E to issue a *mandamus* requiring the trustees to correct or vary their decision to remove the unfair discrimination.

Accordingly, I am not convinced that the trustees have acted *ultra vires* or are in breach of their statutory or common law duties in granting an enhancement to the former members who transferred to the defined contribution funds in 1994 and 1995.

For that reason, Complaint II is dismissed.

Complaint III - The decision to allocate a share of the market value surplus to the employer

In a draft submission prepared by the fund's actuaries for the purpose of section 14(1) (b) of the Act, the valuator, after providing for the transfers out of the fund and the enhancement for former members, describes as the fourth purpose of the scheme as follows:

> **"To provide for the transfer of portions of the remaining surplus in the Nedcor Pension Fund, taking the assets at market value to the Nedcor Defined Contribution Pension Fund and the Nedcor Defined Contribution Provident Fund. These portions are still to be determined and will be transferred to a special reserve account in each of the defined contribution funds. Monies in these reserve accounts will be applied towards the financing of the employer contributions to the respective funds.**

The complainant complains that the transfer of a share of the surplus to a special reserve account in the defined contribution funds would be contrary to the rules in that it would constitute a financial advantage to the employer which the

employer is not entitled to in law.

The document providing for the transfer of a share of the surplus to special reserve accounts in the defined contribution funds was in fact a draft report for discussion purposes with the trustees and the Financial Services Board. The document (annexure "F" to the complaint) was never presented to the Registrar in terms of the Act. The final submission which was submitted to the Registrar in terms of section 14(1)(b) makes no reference to such special reserve accounts.

In two letters addressed to the complainant's attorneys, the respondent's attorney drew attention to the fact that there was no intention to transfer a share of the surplus to special reserve accounts. In a letter dated 14th January 1998 (annexure "BB" of the complaint) the respondent's attorneys stated:

> **"No part of the market value surplus is being directly or indirectly allocated to the employer. To the extent that the whole of the market value surplus is not being allocated in terms of the restructuring proposals, the balance remains as a reserve to underpin the future obligations of the fund."**

In a subsequent letter dated 23rd February 1998 (annexure "R9") the respondent's attorney states:

> **"No application in terms of section 14(1) in respect of the transfer of any assets of the fund to special reserve accounts in the defined contribution funds has been made and nor will such application be included in the set of applications being submitted in terms of the current restructuring proposals. It follows that no such transfer has been implemented."**

On this basis, the respondent has argued that there is no factual basis for Complaint III and it should therefore be dismissed.

In oral argument, however, Mr Kennedy maintained that the complaint went further than the issue concerning the transfer of a share of the surplus to a

special reserve account in the defined contribution funds. In the founding complaint, Complaint III is headed *"Decision to allocate a share of the market value surplus to the employer"*. Since August 1997, the complainant has consistently maintained that in law, and in terms of rule 22 of the rules of the fund, the employer is not entitled to claim any monies of the fund. It argues that the payments made to the fund by the employer constitute part of the member's remuneration package and may not revert to the employer.

Essentially, therefore, the complaint is that the trustees have taken a decision to allocate approximately 25% of the market value surplus to the employer. The evidence certainly discloses some desire to transfer that amount into the defined contribution funds to permit the employer to take a contribution holiday in those funds. However, when it was realised that such a transfer might fall foul of the *Tek* decision, the trustees instead allocated the surplus for use by the employer in the defined benefit fund.

The trustees' intentions in relation to the remaining portion of the market value surplus are fairly self-evident. In paragraph 7.4 of the resolution of 13th October 1997 the trustees make the following observation:

> "Having regard to the fact that some 75% of the market value surplus is to be allocated to in-service members who go defined contribution and pensioners in this restructure, (sic) the trustees regard it as fair for the employer to benefit from 25% of the market value surplus. Furthermore, the employer will only benefit from the surplus if and to the extent that it is not required to underpin the benefits provided for in terms of the rules of the Nedcor Pension Fund, and the employer will continue to underwrite pension benefits (for e.g. In the event of failure of either of the insurers)."

The complainant claims that by this decision the trustees have fettered their discretion in advance in relation to the uses of the surplus. The decision may lead to a reduction of the pot substantially at the expense of inflation related increases

for the pensioners.

Furthermore, he maintains that the decision to allocate R140 million of the surplus to the employer contravenes rule 22 of the funds rules. Rule 22 provides:

> **"Except as otherwise provided in rule 20, no monies of the fund will revert to or become the property of the employer."**

Despite its apparent initial intentions, it is apparent from the two letters cited above that the respondent has subsequently taken the position that no surplus is being directly or indirectly allocated to the employer.

In paragraph 20.4 of the respondent's reply, the respondent further sets out its intention in relation to the balance of the market surplus. It states:

> **"In any event, it should be repeated that no portion of the market value surplus will be accessed by the employer in terms of the current proposals otherwise than by way of a legitimate reduction in contributions or contribution holiday. This position may of course change if the proposed amendment to the Act creates the possibility of alternative means of accessing such surplus."**

In short, the respondent is taking the view that it is entitled to compete with the members of the fund for the surplus in accordance with the principles laid down in the *Tek* decision and in the proposed amendments to the legislation.

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

24. 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.

25. 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.

26. 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.

27. 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.

28. 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 ensure to the benefit of the pensioners and active members of the pension fund at the time of the transfer."

29. 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.

As far as the proposed "repatriation" legislation is concerned, this legislation has arisen as a result of the deliberations of a task group set up by the Pension Funds Advisory Committee. The 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.

Hence, before the employer in the future can derive any real benefit from the market value surplus remaining in the defined benefit fund after the restructuring exercise, the trustees shall be obliged to exercise their discretion in accordance with the dictates of the *Tek* Judgment or the proposed repatriation legislation, depending on whether they wish to secure a contribution holiday or a repatriation.

In passing it should be noted that the *Tek* decision has been taken on appeal. One of the arguments which will be advanced is that all surplus in a defined benefit pension fund is attributable to over-contribution by the employer. 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. In the words of Mr Peter Milburn-Pyle, the Chief Actuary of the Financial Services Board, in a paper delivered at the Pension Lawyers Association conference in February 1998, titled *"The Tek Corporation Case - The FSB's View"*:

> **"The employer's contribution obligation, in other words, is no more than to**

keep the funds assets and liabilities balanced, and to absorb the effect of actual experience differing from that assumed by the funds actuary when performing his various calculations. This in turn means that if a reassessment of the funds financial condition shows that the fund's assets have become greater than the fund's liabilities (i.e. the fund has developed a surplus), the employer's current contribution may correctly be reduced or temporarily suspended in order to restore the balance between assets and liabilities, the contributions that would otherwise have been paid being drawn from the surplus assets until this surplus have been exhausted.

And this applies irrespective of the source of the surplus assets. To restrict the extent to which surplus can be used for this purpose, solely on the grounds of the origin of part of the surplus, as the *Tek* Judgment appears to do, would perpetuate a situation where the assets exceeded the liabilities instead of balancing them, and force the employer to pay a higher contribution than his strict obligation in terms of the fund's rules."

This argument, of course, begs the question as to what precisely in law the employer's strict obligation is. Some would argue that the employer's obligation is to contribute to the fund so much as the actuary says that it should.

Be all this as it may, until such time as the High Court decision in *Tek* is overturned, if at all, trustees would be well advised to observe its prescriptions for allocating any part of the market value surplus to the employer.

It is the respondent's contention that the source of at least part of the surplus is attributable to over-contribution on the part of the employer. The only evidence it has tendered in this regard is the written opinion of Mr Brown, an actuary in the employ of Alexander Forbes. In annexure "R17" to the respondent's reply, Mr Brown makes the following comment:-

"Thus the market value surplus has essentially arisen because of increases

> in the value of investments over the years. However, it should be borne in mind that, had it been possible to predict these movements perfectly, the employer contribution rate could have been adjusted accordingly so that there would be no surplus at any point in time. In this sense the whole surplus could be attributed to employer over-contribution. Even if one takes the view that some of the surplus could be attributed to the member contributions, there is still a strong argument for saying that at least half of the surplus has resulted from employer contributions and that therefore the employer has an interest in the distribution of at least that amount."

It will be seen immediately that in the first part of this paragraph Mr Brown subscribes to the views of Mr Milburn-Pyle. The second sentence serves as a justification for a contribution holiday in accordance with line of reasoning followed in the *Tek* judgment.

Much of the aforegoing discussion may strictly speaking not be of direct relevance to determining this part of the complainant's complaint. Mr Kennedy has argued that "the purported entitlement of the employer to a significant share of the surplus has already been recognised by the respondent". This may be so. However, such a recognition is not the same as a binding decision. Paragraph 1.7 of the trustees' resolution of 13th October 1997 and the proposals flowing from it simply make the point that the actuary can recommend a reduction in the employer contribution if there is sufficient surplus in the fund.

Yet the employer has in fact been on a partial contribution holiday since the last valuation dated September 1995. The most recent interim valuation at 30 September 1996 indicates that the required contribution rate by the employer should be 18.15% of pensionable salaries. The rate actually being paid by the employer is 13.45% of pensionable salaries. In the 1996 interim valuation the valuator concludes:

> "The above still means that there is a shortfall of contributions amounting

> to about R18 million per annum based on the payroll taken into account in the valuation. This is still comfortably covered by the excess at the valuation date of the market value of the assets over the derived value, which excess is likely to be even greater at the present time. However, this excess could be severely reduced in the event of a major market setback. Nevertheless, we do not believe that a further increase in contributions is required at this point in time."

Unfortunately the implications of this matter were not explored at the hearing. As stated, the only evidence that part of the surplus is attributable to over-contribution, is the report of the actuary claiming that at least 50% of the remaining surplus is so attributable. This would amount to a figure of about R300 million which is therefore in excess of the R18 million per annum contribution holiday currently being enjoyed by the employer.

The complainant has produced no evidence or argument to counter the allegation that at least R300 million of the surplus is attributable to over-contribution by the employer. Instead it has taken the position, to quote from counsel's heads of argument, that "the surplus should be available for the sole purpose of enhancing members' benefits". Whatever the merits, morality or equity of such a view, it plainly is not consistent with the approach laid down in the *Tek* decision, by which, as an inferior organ of state, I am bound.

Accordingly, I find that no final decision has been taken by the trustees allocating the remaining market surplus of R140 million to the employer. Insofar as the trustees have, in accordance with the recommendation of the valuator, permitted the employer to be on a partial contribution holiday their decision is not in breach of their fiduciary duties in that the contribution holiday is based on a surplus that derives from employer over-contribution.

Moreover, accepting that the employer is entitled to a contribution holiday on the back of past over funding, as in the *Tek* decision, such a contribution holiday does not result in the employer gaining a financial advantage from the fund in

violation of section 1 of the Income Tax Act 58 of 1962 or of rule 22 of the fund's rules. No monies of the fund are reverting to the employer nor are monies of the fund becoming the property of the employer. Rather in accordance with rule 8.1 of the fund's rules the rate of the employer contribution is being determined by the valuator of the fund in such a manner to take account of the over-contribution by the employer in the past.

The extent to which the employer shall be entitled to benefit from the surplus by way of a contribution holiday will be determined by the extent of its over-contribution. The evidence available suggests that the employer may be entitled to request a contribution holiday to the value of about R300 million at the current valuation. The contribution holiday since 1996 is at a rate of R18 million per annum. At this rate the employer's entitlement to benefit from the remaining surplus can eventually exhaust itself. Moreover, the extent to which the employer has benefited from a contribution holiday prior to 1996 is not clear from the evidence. Without additional evidence and further argument on the matter it is impossible to definitively delineate the quantum of the employer's entitlement.

Suffice it to say at this stage, on the evidence available, the trustees are not in breach of their fiduciary duties in allowing the employer a contribution holiday by utilising that part of the surplus derived from the employer's over-contribution. Nevertheless, one may expect the trustees henceforth to be especially vigilant in ensuring that the balance of the surplus is utilised to underpin the benefits provided for in terms of the rules, including future pension increases.

For the aforegoing reasons, the trustees have not exceeded their powers, nor have they breached their fiduciary duties and nor are they guilty of maladministration.

Accordingly, Complaint III is also dismissed.

Complaint IV - Decision not to increase pension to 100% of CPI prior to distributing the surplus

The complainant's fourth complaint goes to the heart of the issue between the complainant and the respondent. The complainant avers that he has a reasonable expectation that the trustees will exercise their discretion in favour of increasing the amount of pensions payable to pensioners to off set the possible depreciation in the value of the pensions in terms of rule 24.1 of the fund's rules. The trustees' decision to distribute the surplus in the manner proposed in the restructuring proposals, without first ensuring that the pensioners are protected against depreciation in their value of their pensions, it is argued, is an improper exercise of their powers under the rules of the fund.

Rule 24.1 reads as follows:

> **INCREASES IN PENSIONS**
>
> **On the advice of the valuator, the trustees may from time to time at their discretion, increase the amount of pension payable to any person in terms of these rules to off set the possible effect of depreciation in the value of the pension.**

The complainant maintains that the pensioners' reasonable benefit expectations under the circumstances in which the defined benefit fund finds itself are:

30. an upward adjustment of all pension to compensate fully for the increase in the consumer price index from the time of retirement;

31. that a fully or closely indexed pension will be forthcoming in the future; and

32. that the loss of the defined benefit arrangement for a defined contribution one be compensated for by an appropriate enhancement of the actuarial reserve transferred to the Old Mutual

and Sanlam;

The last point raised by the pensioners is unfounded. The restructuring proposals do not involve a loss of a defined benefit arrangement for the pensioners. As already outlined above, the respondent is not buying individual policies for each pensioner (Although this will become possible under the proposed amendment to rule 25, but only on application by individual pensioners). Nor is the respondent transferring the actuarial reserve of each member (which is the liability of the respondent to the member) to Old Mutual and Sanlam. The respondent remains liable and the employer continues to underwrite the fund's obligations. In other words, no transfer of business in terms of section 14 of the Pension Funds Act, 24 of 1956, to the insurers will take place. Hence , the comparison between the investment in the policies with the insurers to cover the fund's obligations to the pensioners with the transfer of active members from the defined benefit fund to the defined contribution funds is misplaced. The pensioners remain members of the respondent and are entitled to the defined benefits. No enhancement or sweetener is required because they bear no greater risk than they currently bear under the rules. The enhancement paid to the members transferring to the defined contribution funds is precisely because with that transfer they assume the risk of future investments and investment returns.

The respondent's response to the pensioners' claim to have reasonable benefit expectations of an upward adjustment of all pensions to compensate fully for the increases in the consumer price index from the time of retirement and the claim to a fully or closely indexed pension in the future is threefold.

Firstly, it maintains the pensioners have indeed received an upliftment of their pensions to match the consumer price index. The trustees believe that the enhancement of 18% as well as the annual consumer price index adjustment of 9% will have the effect that most of the pensions will be adjusted to compensate fully for the increase in the consumer price index from time after pensioners' retirement. At the meeting between respondent and the Pensioners Association

on 15th October 1997 the respondent was prepared to concede that if the enhancement of the pensioners' benefits did not compensate fully for the increase in the consumer price index from the time of retirement, the fund would top up individual pensions to bring this about.

On the other hand, the pensioners maintain to allocate the whole or part of the 18% enhancement to the cost of the overall consumer price index adjustment perpetuates a disparity between retired and active members. This and other aspects of the complaint seem to be premised on the assumption that the complainants have a right to a pension adjustment and a right to a share in the surplus.

Rule 24.1 plainly does not grant such a right to pensioners. The rule gives the trustees a discretion to increase pensions, which discretion should be exercised properly. At most, therefore, the pensioners have a legitimate expectation that the trustees will take the consumer price index into account when exercising their discretion. In relation to the surplus, the members of a defined benefit fund may legitimately expect the trustees to exercise their discretion in distributing the surplus in accordance with the principles of good faith and in a fiduciary manner. Obviously, the larger the surplus the greater the expectation that it may be applied towards pension increases. In deciding what is just and equitable in the distribution of the surplus, the trustees properly ought to have regard to, and evaluate, the possibility that all or part of the surplus will one day prove to be a benefit for the members of the fund. See *Stannard v Fisons Pension Trust Limited* [1992] IRLR27@34.

From the evidence it appears that the various enhancements in transfer values resulting in a utilisation of 75% of the market value surplus have been arrived at after serious consideration by the trustees taking advice from their actuaries. The distribution of 75% to members, while retaining the balance in the defined benefit fund as an adequate cushion in respect of future obligations is considered by the trustees to be the most prudent course to be followed. An analysis of the

distribution of the surplus reveals that R174 million is allocated to enhancements for pensioners and deferred pensioners, R110 million to the former members, who transferred during 1994 and 1995, R162 million to in-service members and R141 million to remain within the fund for the use of the employer and to underpin future obligations. As such, the trustees appear to have carefully weighed up the conflicting interests of the different constituencies within the fund, have applied their minds to the question, taking into account all relevant considerations and have not taken into account any irrelevant considerations. More particularly, the fact that the former members had been transferred to the defined contribution funds under a mistaken supposition is a relevant consideration properly taken into account by the trustees in exercising their discretion to distribute the surplus and computing the amount to be allocated to pension increases. Additionally, out of a total of approximately 9000 interested parties, only about 25 have objected to the basis of the allocations.

The second point raised by the respondent in relation to this complaint touches upon the nature of my powers. The respondent contends that on a proper interpretation of the Act, the Pension Funds Adjudicator has jurisdiction only to consider the legality or regularity of the decisions of trustees (i.e. a type of review jurisdiction). The argument maintains that in the absence of an allegation of illegality, of gross irregularity, or gross unreasonableness, the Adjudicator should not interfere with the merits of a decision of the trustees. Complaint IV can be construed as an attack on the merits of the decision of the trustees in awarding pension increases. The complaint, so it is argued, attempts to constitute the Adjudicator as the "super trustee" of all pension funds. In effect the complainant is requesting me to substitute the distribution plan of the trustees with a distribution plan taking the form of an equal percentage increase in the actuarial reserve of each in-service member, retired member, deferred pensioner and dependants prior to the transfer of this and the underlying assets to one of the defined contribution funds. The respondent argues that were I to grant such relief I would effectively be allowing an appeal against the merits of the trustees' decision.

The respondent's contentions on this point are not entirely well founded. The relief sought by the complainant is in fact not an appeal. What I am asked to do is to review the reasonableness of the trustees' decision. Trustees' decisions are akin to administrative law decisions. The respondent's attempt to limit my powers of intervention to gross irregularity or gross unreasonableness are predicated on outmoded administrative law doctrine. Prior to the adoption of a fundamental Bill of Rights in 1994, South African administrative law doctrine regarded unreasonableness, in itself, as not being a reviewable defect. Unreasonableness was material only insofar as from it may be inferred the existence of some other deficiency in the decision - symptomatic unreasonableness. Plus, it followed, that a merely ordinary degree of unreasonableness was not sufficient to nullify the decision.

This doctrine has now been ousted, originally by section 24(d) of the interim Constitution of 1993, and later by section 33 of the Constitution of 1996 which confers on everyone the right to administrative action that is lawful, reasonable and procedurally fair. Section 7 of the Constitution requires the state (including the Pension Funds Adjudicator) to respect, protect, promote and fulfil the rights in the Bill of Rights. Moreover, section 8(1) provides that the Bill of Rights applies to all law and binds the legislature, the executive, the judiciary and all organs of state (including the Pension Funds Adjudicator). Relying on these provisions, I am of the view that unreasonable decisions by trustees of pension funds will constitute improper exercises of power or maladministration as contemplated in the definition of a complaint in section 1 of the Pension Funds Act.

Such an interpretation, it must be said, does not grant the Adjudicator a licence to second guess the substantive policy choices which properly fall within the prerogative of trustees. The primary purpose of an investigation into the reasonableness of trustee decisions will still be to test the soundness of the process of deciding which went into making the decision, The idea is to introduce

an ethic of justification on the part of the trustees. The late Professor Mureinik in *"A Bridge to Where? Introducing the interim Bill of Rights"* (1994) *SAJHR* 31@ 41 summarises the correct approach to reviewing the reasonableness of administrative decisions. He suggests that an administrative (or trustees') decision cannot be taken to be justifiable or reasonable unless:

33. the decision-maker has considered all serious objections to the decision taken and has answers that plausibly meet them;

34. the decision-maker has considered all the various alternatives to the decision taken and have discarded them for plausible reasons; and

35. there is a rational connection between premises and conclusions - between the information (evidence and arguments) for the decision maker and the decision taken.

On the facts placed before me, and for the reasons set out above, I am satisfied that the trustees have justified their decision as reasonable. The 27% enhancement to pensioners restores the purchasing power of their pensions to take account of the consumer price index since retirement. The differential treatment of transferring members and former members is justified by virtue of their assuming a higher risk. There is a real likelihood that future pension increases will be met out of the bonuses declared annually by the insurers. In the event that the declared bonuses fall short of the consumer price index, there remains a significant surplus in the defined benefit fund which the pensioners can legitimately expect to be applied to meet any shortfall.

In the circumstances, I am satisfied that the decision of the trustees not to increase the pensioners' pensions to 100% of the consumer price index prior to distributing the surplus is reasonable and justifiable.

Finally, in relation to this complaint, the respondent maintains that as the

complaint was not raised in the letter of complaint required by section 30A(1) it should be dismissed for this reason. The argument was not pressed by Mr Du Plessis during oral argument. Consideration of the complainant's letter of 29th December 1997 reveals that whilst the complaint was not specifically raised in exactly the same terms as the complaint lodged in terms of section 30A(3), the substance of the complaint is covered by the reasons put forward for rejecting the restructuring proposals. These include:

> **"(c) the inequitable and arbitrary distribution of the surplus as between pension members and active members;**
>
> **36. the failure to give full recognition to the reasonable benefit expectations of pensioners and to comply with the established practice of the fund.**

On a holistic approach, therefore, the complaint has been properly lodged.

Nevertheless, because I am of the opinion that the decision of the trustees was reasonable, Complaint IV is also dismissed.

Complaint V - Amendment to Rule 17 *Bis*

In this complaint the complainant alleges that the trustees' decision to amend rule 17*bis* to give effect to the proposal to enhance the transfer values of the former members is in excess of their powers under the rules, alternatively an improper exercise of their powers and in breach of their fiduciary duties.

The complaint about the amendment is that it seeks to give the trustees the power to allocate and transfer benefits to persons who are not presently members of the fund. As I mentioned in my discussion of Complaint II, it is questionable whether this amendment is necessary to give effect to the enhancement. In my view, the existing rule in any event gives the trustees the

power to enhance the transfer values of former employees who have transferred to a fund to which the employer is a participating member. It goes without saying that that power must be exercised properly, fairly and reasonably.

The decision to amend rule 17 *bis* was motivated by the legitimate consideration that the former members should not be discriminated against in respect of their share in the surplus which existed at the time of their transfer. Insofar as the amendments accomplish its scheme (albeit that the amendments may be *ex abundanti cautela*) there can be no objection to the trustees' decision. Moreover, there can be no objection to the decision to amend the rule on the ground that it may have been motivated by incorrect legal advice about its necessity from the Financial Services Board or the respondent's attorneys.
On this basis, the respondent is correct in its contention that the rule is unobjectionable in as far as it seeks to empower the trustees to transfer enhancements to the defined contribution funds in favour of transferring members and the former members who transferred in 1994 and 1995.

However, the substitution of the fourth paragraph of rule 17 *bis* is problematic by virtue of its wide terms. The first proviso of the paragraph on a literal interpretation permits the trustees to transfer enhancements in favour of previously transferred members out of a *surplus which did not exist at the time of the transfer*. Benefiting such persons would be contrary to the reasonable benefit expectations of pensioners, members and former members who contributed to the origins of the surplus. Accordingly, the rule requires reformulation. The respondent has conceded this.

In accepting that the fourth paragraph of the amendment to rule 17 *bis* is too widely framed, the question arises as to what relief the complainant is entitled in that regard.

Little purpose would be served by striking down the rule which in all other respects is workable. However, the rule cannot be permitted to stand in its

present form. The appropriate solution is to order the trustees to reformulate the rule within a set time period. Failing which, the paragraph of the amendment shall be declared invalid and shall be set aside. It shall be so ordered below.

Complaint VI - Amendment to Rule 24.2

The complainant complains that the decision of the trustees to amend rule 24.2 in the manner set out in its resolutions dated 6th February 1998 was an improper exercise of their powers in terms of the rules of the fund and has requested me to set aside the decision. Rule 24.2 in its unamended form reads:

> **SUPPLEMENTARY PENSIONS**
>
> **The trustees may from time to time grant supplementary pensions in addition to the pensions in payment in terms of these rules and will for the purposes of this rule include deferred pensions which will become payable when the deferred pensioner reaches the normal retirement age.**
>
> ***In deciding on the level of the supplementary pensions, the trustees will have regard to the official cost of living index in the Republic of South Africa, or other country if appropriate and will consult with the employer and the valuator.*** **The employer will make any additional contributions required to any liability under this rule to the fund.**

The amendment to the rule deletes the italicized first sentence of the ultimate paragraph of rule 24.2.

The amendment aims to diminish the status of the cost of living index as a relevant consideration to be taken into account by the trustees when exercising their discretion to grant supplementary pensions.

The respondent's reason for the amendment is neither clear nor convincing. The members of respondent have a reasonable expectation that the trustees will, in

appropriate circumstances, exercise their discretion in favour of granting supplementary pensions, especially when the fund is in surplus. In doing so, they can be expected to have regard to the official cost of living index. The deletion of this sentence on the basis that the bonuses declared by the insurers will be passed on to the pensioners is contrary to the expressed sentiment that a significant part of the remaining market surplus will be utilised to underpin the benefits of the pensioners in the event of the insurance policies not performing as well as predicted.

The respondent counters by arguing that despite the amendment the trustees retain their power to grant increases and the power to have regard to the cost of living indexes, if in their opinion the bonuses declared by their insurers are insufficient. This may well be true. But given that this is all the rule in its present form requires, one might be forgiven for asking, with some scepticism, why the amendment is necessary at all. The deletion of the obligation to have regard to the cost of living index will furnish some foundation for an argument that the liability of the fund towards its pensioners is met principally by giving them the benefit of the insurance policies. As such, it might be taken as diminishing their legitimate expectation to share in the remaining market value surplus. This would be in stark contrast to the trustees' stated intentions. The rationale for the amendment is hence contradictory. All rule 24.2 requires is for the trustees to have regard to the cost of living index. The trustees maintain that they will continue to have regard to the cost of living index, but seek to delete the obligation to do so. Hence, there is no rational connection between the premises and the conclusion of the argument underlying their decision. Consequently, it is appropriate to stigmatise the decision as unreasonable, and thereby constituting an improper exercise of discretion and maladministration.

For these reasons Complaint VI is upheld and the decision of the trustees to amend rule 24.2 is hereby set aside.

RELIEF

The order of this tribunal is:

37. Complaints I, II, III and IV are dismissed.

38. Complaint V partly succeeds in the following terms. The trustees of the respondent are hereby ordered to reformulate the amendment to rule 17 *bis* to ensure that the trustees are not empowered to transfer enhancements in favour of previously transferred members to the defined contribution funds out of a surplus which did not exist at the time of their transfer. Such reformulation shall be effected within 30 days of the date of this order whereupon the reformulated rule shall be submitted to this tribunal for further consideration and decision.

39. Complaint VI succeeds and is upheld, and the decision of the trustees of the respondent to amend rule 24.2 is hereby set aside.

40. With the agreement of both parties, no order is made for costs.

DATE AT CAPE TOWN THIS 20TH DAY OF MARCH 1998.

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PROF JOHN MURPHY

PENSION FUNDS ADJUDICATOR