

IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO: PFA/WE/494/99/JM

In the complaint between:

ANDREW WILLIAM RABE

Complainant

and

CAPE MUNICIPAL PENSION FUND

Respondent

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

1. This complaint arises out of the restructuring of the Cape Municipal Pension Fund (hereinafter “the fund”) during the course of 1998 and 1999. The parties have agreed that the complaint should be determined on the basis of documentary evidence and written submissions. No hearing has been held.
2. The complainant has been employed with the Cape Town City Council since January 1975 as a surveyor technician and has been a member of the fund for a period of approximately 24 years.
3. The Cape Town Municipal Pension fund was established in 1925 and was constituted in terms of Provincial Ordinance No. 24 of 1919, and then provided for a gratuity and a pension on retirement. The fund and its current rules were registered in terms of the Pension Funds Act on 23 June 1962.

Prior to 1 July 1997, the principal employer in the fund was the Cape Town City Council and membership of the fund was open only to its employees. On 1 July 1997 many of the

members of the fund were transferred to newly created local authorities in accordance with the provisions of the proclamation 12 of 1997 (Western Cape), promulgated in terms of the Local Government Transition Act 12 of 1994. As from that date, the fund became a multi-employer fund.

With effect from 1 March 1998, the name of the fund was changed from Cape Town Municipal Pension Fund to Cape Municipal Pension Fund in order to reflect the broader membership.

4. During the course of 1998 the fund undertook a restructuring exercise following on negotiations between the participating employers and employee representatives. As a consequence of their negotiations, it was agreed that the fund would introduce a defined contribution section and would provide benefits on a defined contribution basis for all employees becoming members on or after 1 July 1998. Existing members of the fund at that date were granted the option of having their benefits converted to the new basis or retaining their existing defined benefit status. The effective date of conversion was 1 July 1998. However, members were given an option period originally terminating on 30 September 1998, later extended to 30 October and ultimately to 28 February 1999 in order to exercise their options.
5. In accordance with the principle of freedom of association, employees were also granted the opportunity to transfer out of the fund to the SAMWU or IMATU Pension Funds.
6. The complainant contends that he has not had a proper opportunity to exercise his option to transfer from the defined benefit section of the fund to the defined benefit contribution section of the fund and seeks an order directing the respondent to take all necessary steps to allow him to transfer from the defined benefits section to the defined contribution section of the fund.

7. Throughout the negotiations attendant upon the restructuring exercise the complainant was a member and was represented by the Cape Metropolitan Services Union (the "MSU") which has been actively involved in pursuing concerns and queries raised by its members in an attempt to obtain clarity on issues of concern prior to making an option decision. Although the MSU is not recognised as a trade union by the City of Cape Town for collective bargaining purposes, both the employer and the fund have endeavoured to consult with it and to enter into good faith discussions with it concerning grievances raised on behalf of members.
8. As stated, originally the period for allowing members to make an election was due to expire on 15 September 1999. However, due to the volume of queries and concerns raised by members in relation to a variety of issues, this period was extended to 30 October 1998.
9. During September 1998, the MSU addressed correspondence to the fund highlighting members' queries pertaining to the restructuring process and requesting confirmation on the tax implications associated with the restructuring process.
10. The complainant's principal contention is that he has not been able to exercise a proper option because there was no clarity on the tax consequences of a transfer from the defined benefit section to the defined contribution section.
11. From the correspondence submitted to me it is apparent that there was considerable confusion on the part of all concerned, including the South African Revenue Service ("SARS"), concerning the tax consequences of a transfer between the two sections. Much of the cause of confusion was the fact that the withdrawal benefits in the defined contribution section were particularly generous and served as an inducement to transferring members to resign. Thus, if a member resigned or was dismissed prior to his normal retirement date (in most cases 65), the member was entitled to the full amount of his share account as at the date of such dismissal or resignation. Prior to March 1999 such an amount was totally tax free by virtue of the fund being a public sector fund. Even subsequent to

March 1999 such lump sums are taxable only to the extent of accruals to the benefit after that date.

12. By comparison, any member retiring out of the defined contribution section (as opposed to resigning) on attaining the appropriate retirement age would be entitled to commute a maximum of one third of the pension and would receive the balance as an annuity taxable at marginal rates.
13. In the defined benefit section withdrawal benefits are particularly ungenerous being pegged at a return of the whole amount of the member's contribution plus 4% of such amount for each completed year of contributory service exceeding five years. Employees with more than ten years service may elect to become deferred pensioners. Retirement benefits are the standard defined benefits, being a pension calculated in accordance with a formula based on a percentage of earnings for the period of service.
14. This benefit structure with its attendant tax consequences, one imagines, put a number of older members into something of a dilemma, and in order to get the advantage of a substantial tax free withdrawal benefit, many older members appear to have considered resignation. A difference of opinion arose between the fund and the SARS about taxing members who wanted to resign and seek re-employment and also in relation to the taxation of the benefits of members over the age of 55 who opted to resign instead of retire in order to obtain the advantage of the lump sum withdrawal benefit.
15. On 7 September 1998 the legal manager of the fund addressed an e-mail to Mr Vlok Symington of the SARS seeking certain clarification. The e-mail read as

follows:

Tax-free status of lump-sum benefits - public sector pension

We are receiving numerous enquiries from our members regarding the above. Some have

contacted the local offices of the Revenue Service and have been informed that the above is only applicable as lump sums payable on retiral (i.e. not on resignation or dismissal). In other words that "Formula C" only applies to retiral - should they resign or be dismissed their entire lump sum will be taxed.

Would it be possible to receive a formal directive or instruction from yourself in order to clarify the situation and thus allay the fears of our membership.

16. On 16 September 1998 Mr Symington replied to the e-mail as follows:

Formula C also applies to the resignations and dismissals. There is no doubt about that. But the Receivers of Revenue which you refer to have advised me that members of the fund told them that they (the members were advised by the fund that they are entitled to resignation benefits while they remain in service (sic). SARS cannot go along with something like this. If this is indeed the case and the employer is going to allow these people to "resign" from employment just to be "re-employed" the next day, I will certainly do my best to argue that the fund is not a pension fund at all and that recognition as such must be withdrawn.

It should, furthermore, be noted that members who become entitled to benefits while they effectively remain in employment of the same employer will be subject to tax or two-thirds of the benefit in accordance with the revised paragraph (eA) of the definition of "gross income" in section 4 of the Income Tax Act.

17. The SARS's concerns were further spelt out in a letter addressed to the fund by the Receiver of Revenue on 7 October 1998 which reads as follows:

I received numerous enquiries from your members regarding the above.

In general, a lump sum payable from a par (a) fund will be tax-free until 28 February 1999. As from 1 March 1999 formula C of the Second Schedule to the Income Tax Act will be applied to calculate the taxable portion of a lump sum.

It has come to my attention that some members resigned and were re-employed on a

permanent - or contract basis by the Council. These members will be subjected to tax on two-thirds of the benefits in accordance with the revised paragraph (eA) of the definition of "gross-income" in Section 1 of the Act.

Cases where members resigned after reaching their normal retirement age has been forwarded to the Commissioner's Office for further investigation.

A list of names and ID numbers of those members who have resigned from the fund as well as those who were re-employed on any basis by the Council is to be forwarded to me by 31 October 1998.

18. In subsequent communications it became clear that SARS felt persons over 55 should retire and not resign, otherwise the fund would be acting as a provident fund rather than a pension fund. These communications led to the legitimate concern on behalf of the members and the fund that the SARS could withdraw recognition of the fund and might tax two-thirds of the lump sum in the hands of the members in terms of paragraph (aE) of the definition of "gross income" in the Income Tax Act of 1962.

19. The fund clearly believed that the SARS's interpretation was incorrect. In a letter dated 21 September 1998 addressed to certain members of the MSU, the legal manager of the fund makes the following comments:

The Cape Municipal Pension Fund is a recognised Paragraph (a) fund in terms of the section schedule of the Income Tax Act. We are aware that erroneous information is being disseminated by certain officials of the South African Revenue Service, but the fund has been in contact with Vlok Symington of SARS in Pretoria and he shares our interpretation that lump sum payments prior to 28 February 1999 are tax free. We are awaiting a formal directive from him in this regard. Furthermore our auditors have also confirmed our interpretation of the tax issue.

20. Thus, the MSU members were led to believe that erroneous information was being disseminated by the South African Revenue Service and that the fund was awaiting a formal tax directive or ruling to clarify the position.

21. In an attempt to obtain clarity the MSU instructed its attorneys to address correspondence to the fund shortly before the expiry of the option period on 30 October 1998. The relevant portion of this letter reads as follows:

As previously highlighted, our clients have advised that to date no formal tax directive/instruction has been forthcoming from the South African Receiver of Revenue's office regarding the taxation of benefits should fund members elect to immediately utilise an option to resign.

The writer has been placed in receipt of correspondence emanating from the local Receiver of Revenue's offices in the Western/Northern Cape Region, which appears to indicate that the lump sum benefit, if taken prior to 28 February 1999 shall be regarded as tax-free benefit in accordance with the current and applicable Tax Legislation. We are furthermore advised that the Receiver has indicated that members who merely resign from their employment, only to be thereafter re-employed, will not benefit from the tax-free status applicable to the lump sum payment.

We are accordingly of the opinion that prior to our clients electing to utilise any specific options under the newly restructured Pension Fund, the issue regarding the tax directive should be fully resolved. The potential prejudice that Fund Members who elect to resign on the representations already made by the Fund regarding tax-free packages, only to find that they are liable for tax on their lump sum payments, is significant.

Accordingly, we request your urgent response to the issues highlighted above, particularly in light of the fact that the deadline that Members are confronted with in having to make their allocation, has been set for 30 October 1998.

22. The fund responded to the union's attorneys after the expiry of the deadline by letter dated 6 November 1998 in the following terms.

The letter from Mrs Engelbrecht of SARS to which you refer clearly states that lump sums payable from a paragraph (a) retirement fund will be tax free until 29 February 1999. (sic)

Due to members approaching the Receiver of Revenue to query the above, in spite of

assurances from our Auditors and the clear provisions of the Income Tax Act, the authorities have become concerned that our fund may be actively encouraging members to resign where they are in fact eligible for retirement benefits. Should it become apparent that we are operating as a Provident Fund instead of a Pension Fund they may seek to impose Section 103 Avoidance Provisions.

In reality, although our fund rules provide for withdrawal prior to normal retirement age, which for the majority of members is 65, we require any member over the age of 55 who opts to resign, to complete an indemnity form, and offer counselling covering the various options to be considered. The fact that a member will forfeit his medical aid subsidy should he resign instead of retiring is also emphasized. Our tax consultants and attorneys are pursuing this matter with the tax authorities on our behalf and we are confident that our position is above reproach.

Notwithstanding the above, the fund cannot guarantee that resignations benefits will be tax-free for older members who would have been eligible for retirement. All we can do is state what the current tax law provides. The defined contribution option is not conditional on the basis that resignation benefits will be tax-free. Members are free to choose an option based on various factors, not least of which is a comparison of benefits under the various funds, and their choice should not solely be based on whether the resignation benefits under each.

We have been advised by our tax consultants that should members resign from the fund and receive withdrawal benefits, only to be re-employed by Council, either as an "independent contractor", or otherwise, they may run the risk of being taxed on two-thirds of that benefit. The employer has been advised that this course of action has certain risks attached to it, and that the preferable option would be for the employees in question to extend their notice periods in order to ensure smooth transition.

23. Subsequent to this a series of negotiations were embarked upon in which various proposals were put forward on behalf of the union to the fund and ultimately the option period was extended. In relation to the tax issue the proposal was that the fund should undertake to confirm that all lump sum benefits would be tax free and that should the office of the SARS attempt to declare the pension fund a provident fund and thereby attempt to institute the avoidance provisions of section 103 of the Income Tax Act, the fund would challenge any such directive at the appropriate adjudicative forum on behalf of the affected members. In

addition, the fund was requested to retain liability for the value of any amount due in respect of an adverse tax directive.

24. In a letter dated 27 January 1999 the fund addressed the question concerning the resignation benefits as follows:

24.1 the fund was unable to warrant that the resignations would be tax free in all cases and a directive or ruling was still awaited from the office of the SARS in this regard;

24.2 the fund emphasised that at no stage had it advised members to opt for resignation as opposed to retirement; and

24.3 despite the fund's willingness to challenge any adverse directive received from SARS, the fund could not in any way accept liability for any adverse tax implications.

25. In the same letter, addressed to the union's attorneys, the legal manager of the fund makes the following observation:

Although our auditors concur with our interpretation of the Income Tax Act the Fund has nevertheless informed all members aged 55 and over of the possible risk of taxation and required them to sign an indemnity form prior to receiving any such benefit. It is our view that the decision of a member whether to retire or resign should be based on broader considerations than taxability - for example the medical subsidy from the employer which is forfeited on withdrawal,...

26. The opinion of the auditor is contained in a letter addressed by the auditors to the fund dated 16 September 1998, the contents of which was presumably conveyed to the union verbally. However, the opinion was never actually furnished to the union's legal

representative. The relevant part of this auditor's opinion reads:

I write in response to your facsimile request dated 9 September 1998 and our telephonic conversation on 16 September 1998 to confirm the tax implications of those Cape Municipal Pension Fund members who resign or retire, after transferring from your old defined benefit scheme ("existing scheme") to your newly registered defined contribution scheme ("new scheme").

I set out below the tax implications upon transfer to the new scheme as well as the subsequent resignation or retirement from the new scheme.

Initial transfer by the member to the new scheme

If the new scheme is a paragraph (a) pension fund (i.e. paragraph (a) of the definition of "pension fund" in the Income Tax Act - hereinafter a "public sector fund"), the transferring members' vested rights (see below) will be protected on the transfer of their benefits to the new scheme. Furthermore, the transfer values will only be exempt from tax if the rules of the new scheme does not permit entitlement to a lump sum on retirement in excess of one-third of the actuarial value. If it does, paragraph (eA) of the "gross income" definition will render two-thirds of the transfer value taxable.

Resignation from the new scheme

On the assumption that the new scheme is a public sector fund, the resigning or retiring members' vested rights will be protected. The vested rights referred to above relate to the continued tax-exemption status of any lump sum paid out by a public sector fund in respect of services that were rendered before 1 March 1998. Furthermore, any lump sum paid out between 1 March 1998 and 27 February 1999 will remain tax-free. However, to the extent that a lump sum payment made after 1 March 1999 relates to completed years ending after 1 March 1998, such portion will be taxable.

You confirmed that the new scheme is a public sector fund. As the new scheme was established for the benefit of the employees of a local authority, the new scheme will in my view be regarded as a public sector fund.

To summarise - As the new scheme is a public sector fund, the lump sum payments made to resigning or retiring members prior to 28 February 1999 will be tax-free.

27. After receiving the auditor's opinion, the marketing department of the fund distributed a copy of an information brochure or magazine - "*Fund Talk*" during the course of October 1998, dealing with the taxation concerns. On one page under the heading "**questions and answers**" the following two items appear:

Q. Is it true that my money in the fund will be taxed if I don't resign before 1st March 1999?

A. The CMPF is what is known in income tax law as a "paragraph (a)" fund. This means that it is treated differently to private sector funds. Basically, all your fund benefits up to the 28th of February 1998 are protected from tax. After that date your contributions and investment income will be taxed in the same way as private sector funds. In other words you will pay tax on any full completed years' service after 1st March 1998. Please refer to the attached taxation information and the letter from our auditors, Deloitte & Touche.

Q. I've heard that the Receiver of Revenue's office have said that the benefits are taxable, why?

A. When talking to the tax offices many people do not clarify that they are a member of a local government fund. This is likely to lead to the Receivers office giving the wrong information.

The attached taxation information read as follows:

TAXATION OF BENEFITS IN DETAIL

Unfortunately there are many misconceptions and rumours circulating about the taxation of fund benefits. People have called the Receiver of Revenue's office enquiring if their benefits will be taxed. The Receiver has in some cases said yes as they probably assumed it was a private sector fund.

The CMPF is a fund established by law, i.e. a Municipal Fund, and therefore a paragraph (a) fund in terms of the Income Tax Act. This means that it is taxed differently to private sector funds.

Below is the actual situation (Refer Schedule 2 of the Income Tax Act):

1. Lump sums on service prior to 1 March 1998 are tax protected.
2. Formula C in the second schedule of the Income Tax Act sets out how lump sums will be taxed after 1 March 1998.
3. Tax is applied on the proportion of the lump sum for completed tax years after 1 March 1998, after taking the private sector formulas into account i.e.
Retirement: The greater of R120,000 or R4,500 x number of years fund membership
Resignation: The first R1,800 is tax-free.
4. The taxable amounts are then taxed at your average rate of tax, not a higher or 'marginal' rate. This means that the percentage of tax is what you normally pay on your income.
5. The formula works as follows:

Examples on resignation:

Transfer value (TV) - R100,000 at 1 July 1998 (as per Transfer Statement)

Member is aged 50, with 30 years of service.

Example A resignation on 1 July 1998

Benefit = R100,000 tax-free (no completed service after 1 March 1998)

Example B Resignation on 1 July 1999

Benefit = TV R100,000 plus (for example) 12% growth - R112,000

$$\text{Tax} = 1/31 \times \text{R}112,000 = \text{R}3,612.90$$

R3,612.90 is taxable

$$\text{R}3,612.90 \text{ less deduction of } \text{R}1,800 = \text{R}1,812.90$$

Tax rate is (for example) 40%

$$40\% \text{ of } \text{R}1,812.90 = \text{R}725.16$$

Example C Resignation on 1 July 2000

Benefit = R112,000 at 1 July 2000 plus (for example) 12% growth -
R125,440

$$\text{Tax} = 2/32 \times \text{R}125,440 = \text{R}7,840.00$$

R7,840.00 is taxable

$$\text{R}7,840.00 \text{ less deduction of } \text{R}1,800 = \text{R}6,040$$

Tax rate is (for example) 40%

$$40\% \text{ of } \text{R}6,040.00 = \text{R}2,416.00$$

Notes:

1. You do not have to resign/retire now to get your limp sum tax-free - this will be tax protected in the future.
 2. This is based on current income tax legislation.
 3. Tax on retirement is not really an issue for members with many years of service, as the R120,000 formula applies.
28. The marketing department physically delivered 11,000 copies of these documents, including the auditors opinion, to every cluster and department in the Cape Town City Council and the Cape Metropolitan Council. While there is no direct evidence that the union or the complainant received a copy of these documents, there is a reasonable probability that they did so. In addition, as part of his information pack, the complainant would have received a full comparison of his benefits, including his withdrawal benefits, in

both the defined benefits section and defined contribution section.

29. Subsequent attempts by the union to prevail upon the fund to guarantee the tax consequences were unsuccessful. This was confirmed in a letter addressed by the union's attorneys to the fund dated 26 February 1999, two days prior to the final deadline. However, in the same letter it was confirmed that despite the fund's refusal to guarantee resignation benefits, it nevertheless would allow the MSU members the opportunity to exercise their options at a later date and upon a directive or ruling being received from the SARS concerning the tax issues. This agreement is stated in the following terms:

Further to your telefax of 24 February 1999 the writer confirms your advices that our clients shall remain on the existing fund, being "the old fund" until such time as they might obtain the necessary directive from the receiver of revenue to make application to exercise their election options.

Presumably relying on this agreement, none of the MSU members elected to transfer to the defined contribution section on 28 February 1999.

30. The existence of this agreement was not challenged in subsequent correspondence or by the fund in its response to the complaint. Indeed, the evidence seems to suggest that the fund in a conspicuous and noble attempt to act fairly conceded that there was a need for a directive and went ahead to try and obtain a formal directive from the SARS without any success. The fund endeavoured to clarify the tax consequences by means of e-mail correspondence with Mr Vlok Symington in Pretoria as well as during a visit by one of its senior employees. The SARS failed to provide it with a clear written directive, even after being approached by the fund's auditors, who were of the opinion that the fund was not in contravention of the income tax legislation. Further efforts to resolve the problem were made by means of a letter to the Deputy Minister of Finance setting out the difficulties and requesting appropriate action.

31. In response to the letter addressed to the Deputy Minister, the Deputy Commissioner of the SARS wrote to the legal manager of the fund on 5 February 1999. The relevant part of this letter reads:

As you are aware, paragraph (eA) of the definition of "gross income" in section 1 of the Income Tax Act provides for the inclusion in a taxpayer's gross income of two-thirds of a member's retirement capital in circumstances where a public sector fund has been converted from a fund providing retirement benefits in the form of a pension to a fund providing retirement benefits in the form of lump sum payments exceeding one-third of a member's retirement capital.

While the Cape Municipal Pension Fund continues to provide retirement fund benefits in the form of a pension, the fund also permits members to become entitled to "resignation" benefits even though they are actually retiring from employment to all intents and purposes, which means that the members now have access to their full actuarial interest in the fund by way of a lump sum cash benefit, on retirement from employment.

As a result of this, the provisions of paragraph (eA) are wide enough to subject to income tax two-thirds of each member's retirement capital, and that steps may soon commence to recover the tax from the fund.

We are, however, prepared to reconsider that matter on receipt of confirmation that the fund has, with retrospective effect, changed its rules to prohibit a member who is actually retiring from employment from becoming entitled to his or her full actuarial interest by way of a lump sum benefit.

I would therefore urge you to make use of this opportunity as soon as possible, failing which we will proceed with the recovery of employees' tax.

32. The letter reveals that the SARS were not entirely convinced of their own position, nor were they in possession of all relevant information. In a further attempt to obtain a ruling, the fund's administrative director, Mr Gamieldien, made additional representations which are contained in a letter dated 9 February 1999 addressed to the general manager of the SARS which reads as follows:

Our sincere thanks to you for responding to our letter addressed to the Deputy Minister of Finance. With regard to paragraph two of your letter, we wish to state that under no circumstances does the fund permit members to become entitled to resignation benefits even though they are actually retiring from employment. The rules of the Defined Contribution fund states that on resignation a member becomes entitled to his share account at the date of termination - on retirement a member is entitle to a one-third lump sum and two-thirds of his cash value of pension must be used to purchase an annuity. On retirement the member may elect to purchase his/her annuity from the fund or any other service provider approved by the Board of Trustees.

The normal retirement ages as per the current rules of the Cape Municipal Pension Fund are as follows (see attached copy of extract from the rules). The earliest a member could retire is at age 55. However, members could resign from employment anytime before they reach normal retirement date. The resignation benefit would be taxed in terms of the Income Tax Act. Members who resign from employment do not qualify for annual pension increases as well as the employers (sic) medical aid subsidy whilst in retirement. The fund has taken the opinion, that members would be paid a resignation benefits in terms of the rules of the fund provided, they have not reached their normal retirement date, thus becoming entitled to their withdrawal benefit which is subject to tax in terms of the second schedule of the Income Tax Act.

The fund has requested a clear direction from the offices of SARS with regard to our current practice in respect of members who resign after age 55. Our rules as well as the Pension Fund's Act allows for resignations over the age of 55. The fund has already taken legal advice on this matter. Mr Vlok Symington's office has copies of all the documentation for your reference.

33. Despite the request for a clear ruling, to date the SARS has failed to provide the fund with a formal directive, or according to the fund any proper and full opportunity to state its case. These failed attempts probably led to some justifiable sympathy with members' needs for greater clarity, and hence the concession recorded by the MSU's attorney to extend the period until a directive was obtained.
34. On 12 April 1999 the complainant through his legal representative addressed a request to

the fund to be entitled to exercise his option to transfer to the defined contribution section, six weeks after the lapse of the extended option period and despite the fact that no directive had been forthcoming from the SARS. Various subsequent attempts were made to resolve the issue in which the complainant's employer interceded and eventually the complainant addressed a letter on 8 June 1999 to the trustees of the fund. In this letter the complainant explains his reasons for "postponing" his decision to transfer:

At the outset, one of the most compelling factors in the decision not to immediately transfer was a lack of clarity concerning the possible or potential tax obligations that I might have been subject to with a transfer to the Defined Contribution Fund, particularly given the fact that I had been advised and received confirmation from the South African Revenue Services that there was a potential danger that tax obligations could be imposed on any such transfer.

Numerous efforts were made both by me and my colleagues to the Receiver to attempt to obtain clarity, however, we still await a formal directive indicating that a transfer as aforesaid would fall outside the applicable tax legislation. Furthermore as is evidence from the numerous correspondence between my Trade Union's appointed Attorneys of record and the Fund, it is clear that as of 25 February 1999 no clear position could be guaranteed by either the South African Revenue Services or the fund with regard to the possible tax obligations. Accordingly, and given the situation facing me at the time, I had no option but to elect to postpone making a decision. I believe, as you will note from the facts set out hereunder, that my decision was the only reasonable option available to me at the time.

Further in the letter he explains that he wishes to resign his employment and emigrate to New Zealand. He states that had he been accepted for emigration prior to 25 February 1999, he would have taken the tax risk in transferring to the defined contribution section.

35. At the Board of Trustees meeting held on 27 August 1999 the Board resolved to reject the complainant's application for a transfer from the defined benefit section to the defined contribution section of the fund on the grounds that he had had sufficient opportunity and information at his disposal to exercise his option properly.

36. The complainant's challenge to the trustee's decision is formulated as a claim that the trustees are in breach of their duties to ensure that adequate and appropriate information is communicated to members informing them of their rights and benefits. In the alternative it is claimed that the fund has failed in its duty to act in good faith and with impartiality with respect to all members. Additionally, there could be some argument that the board is in breach of its duty under 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 provisions of the Pension Funds Act are protected at all times especially in the event of a restructuring of the fund.
37. In my opinion none of these arguments is sustainable. If anything the board has exceeded the call of duty and the evidence shows that the fund acted consistently with its statutory duties, and indeed deserves to be commended for so doing. It went out of its way to clarify the confusion about the tax issue. It sought and obtained an opinion from its auditor which it circulated together with illustrative information to the entire membership. It went further and visited the offices of the SARS and even sought the intervention of the Deputy Minister of Finance. However, it was not prepared to guarantee the tax consequences of the transfer. I would wholeheartedly agree that it was not obliged to do so. Indeed, to have furnished such a guarantee could have proved highly prejudicial to the other members of the fund. Nevertheless, it did its level best to obtain full information from the SARS and communicated what in my opinion was the correct legal advice.
38. By comparison, the MSU's approach to the problem was less than satisfactory. Its attitude was overly insistent and intransigent. It does not appear to have sought and obtained independent tax advice to advance the interests of its members. It proceeded on the false assumption that its handful of members were entitled to a guarantee of a particular tax consequence. Moreover, it drew no distinction between the position of its members over the age of 55 and those younger and went ahead and conflated a number of issues. In acting in this way it exposed its membership to considerable adverse financial risk.
39. In the case of the complainant, the tax position is in fact quite simple. He is under 55 years of age. Therefore, if he transfers to the defined contribution section, he qualifies for a more

generous lump sum resignation benefit, the amount accruing before March 1999 being tax free with a minimal tax liability on amounts accruing thereafter. Much of the correspondence, the *Fund Talk* magazine, the correspondence from the SARS and the personal benefit comparison contained in the comprehensive options package distributed by the fund would have made this abundantly clear, if not to him, then certainly to his trade union. There may be some confusion about the tax consequences should the complainant resign and successfully seek re-employment. But I doubt he ever genuinely entertained such an intention.

Now that he is emigrating to New Zealand, the complainant knows only too well that his decision not to transfer to the defined contribution section was especially unwise. A cursory glance at his illustrative benefit comparison makes that fairly obvious.

Were it not for the fact that the negotiations between the MSU and the fund had secured him additional rights I would have had little hesitation in dismissing his complaint and allowed him to endure the extremely adverse financial consequences of his imprudent intransigence.

However, amidst all the confusion, much of which was more apparent than real, the MSU's attorney succeeded on 25 February 1999 to secure an agreement that the members would be given a further option to make an election in the period between that date and the eventual date on which the SARS issued a formal direction. In terms of the letter of that date (see para 26 above) the option was left open "until such time as they might obtain the necessary directive from the receiver of revenue". A reasonable interpretation of such a term is that the option could be exercised any time before the directive was issued. The real complaint, therefore, in this instance is whether the fund is obliged to honour that undertaking. As such, the complaint does not concern a breach of duty or maladministration by the fund, but is rather a dispute of fact and law.

40. The existence of an agreement to extend the option period for the MSU members is not as

clear cut as one might wish. Nevertheless, in an adjudicative process relying exclusively on documentation and written submissions, I am required to make a ruling on the limited information and evidence at my disposal. The letter of 26 February 1999 written by the MSU's attorney and in particular the passage quoted in paragraph 26 above is the strongest indication of such an agreement. The confirmation of the "advices" was not challenged contemporaneously by the fund, nor was the complainant's reliance upon it in his complaint questioned by the fund in its response to the complaint.

41. Additionally, the complainant's failure to transfer to the defined contribution section was so evidently contrary to his best interests that I can only assume that he was advised by the union that the period for exercising his option had been extended by agreement. His apprehension about his tax position was unfounded, but given the poor advice he seems to have received from his union and the lack of clarity on the side of the SARS, he opted to proceed cautiously. Accordingly, I am inclined to give him the benefit of the doubt and to afford him another opportunity to exercise his option. In view of the devastating financial consequences of dismissing his complaint, this too is the fairest solution. Likewise, the fund in the course of the restructuring would have foreseen the contingency of an enhanced withdrawal liability and will be funded accordingly.

42. The order of this tribunal is as follows:
 - 42.1 The decision of the fund's board of trustees that the complainant not be allowed to transfer from the defined benefit section to the defined contribution section is hereby set aside.

 - 42.2 The fund is ordered to take all steps, including, if necessary, the amendments of its rules to permit the complainant to transfer from the defined benefit section to the defined contribution section.

 - 42.3 The fund is directed thereafter to allow the complainant in accordance with an

option properly exercised to transfer from the defined benefit section to the defined contribution section of the fund.

DATED at CAPE TOWN this 13th day of SEPTEMBER 1999.

John Murphy

Pension Funds Adjudicator