In the complaint between:

Barry J Smith  
Complainant

and

ZAI Provident Fund  
First Respondent

ZAI Consultants (Pty) Ltd  
Second Respondent

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Determination in terms of Section 30m of the Pension Funds Act of 1956

Introduction

1. This complaint relates to the calculation of a retirement benefit payable to the complainant in terms of the rules of the first respondent. The complainant claims that he suffered prejudice as a result of the improper application of the rules by the respondents.

2. The parties have been given ample opportunity to comment on each other’s submissions and I am satisfied that the provisions of section 30F of the Act have been complied with. I am happy that nothing further would be gained from the holding of a formal hearing, and no such hearing has been requested by the parties. My determination, therefore, is based on the written submissions of the parties together with the report of my senior investigator, Ian McDonald, who investigated the complaint on my behalf.
Background to the complaint

3. The complainant was retired from the second respondent at the age of 60, with effect from 30 November 1998, and was paid a retirement benefit from the first respondent in terms of its rules. Normal retirement age is age 55 and the complainant received a benefit in terms of rule 28(a)(ii), which states that a full benefit will become payable where the member on reaching retirement age was retained in service and retires subsequently.

4. Rule 27 sets out in detail how a full benefit is made up, and can be summarised as.

4.1 the total amount contributed to the fund by the member and by the employer on his behalf, plus

4.2 the share of the profits allocated to the member up to and including the last investigation made in terms of rule 26, together with an equal amount from the General Suspense Account of the fund, plus

4.3 interest on the sum of 4.1 and 4.2, at a rate determined by the committee of management of the fund from time to time, for the period from the preceding investigation to the date the benefit becomes payable.

5. Rule 26 says that an investigation of the fund=s finances will be undertaken on the last business day of each June and December and details the manner in which these investigations will be undertaken. This rule caters for the calculation of the book value of the assets held by the fund and for increases and decreases in book value to be credited and debited to an Investigation Account, as the case may be. The Investigation Account is also credited or debited, as appropriate, with:

5.1 capital profits realised and capital losses sustained as a result of the sale of any of the fund=s assets;
5.2 all dividends received by the fund;
5.3 all interest earned on the assets of the fund, less the total amount paid to members in respect of interest,
during the preceding six months.

6. On completion of the investigation, half of the net balance in the Investigation Account is allocated amongst the members in proportion to the total amount standing to the credit of each member’s account on the investigation date, by way of a credit or debit to the members account, as the case may be, and the other half of the net balance is transferred to the General Suspense Account.

7. The complainant’s benefit was paid to him, after deduction of tax, in accordance with a calculation sheet dated 7 December 1998 which showed his full benefit as at 30 November 1998 to be R881,345.62, considerably lower than the figure of R967,660.22 that had been advised to him in a statement of his accumulated contributions as at 30 June 1998.

8. After discussing the calculation of the benefit with Mr Rodney Brand, a member of the committee of management of the fund, he wrote to the chairman of the committee of management, Mr Alastair Johnston, on 8 March 1999 explaining his concerns and asking the committee to review his benefits in the light of the more accurate figures, then available, of actual fund experience to the end of December 1998.

9. In his response dated 1 April 1999, Mr Johnston confirmed that the complainant’s request had been tabled at the fund’s AGM the previous week and that a unanimous decision had been reached not to review his benefit.

10. He went on to say that it had been found that the requirement in the rules of the fund that it be revalued only twice a year had been found to have a serious impact
The members of the fund took a decision at the AGM of the Fund held on 18 March 1994 to alter the method of valuing the equities of the Fund. The minute of what was agreed is as follows:

"The chairman presented a number of slides which showed how the Fund had performed over the last sixteen years. The comparison of book value with market value of the Equities showed large fluctuations, it was agreed that revaluation of the Equities be undertaken at 3 month intervals. This was expected to ensure fairer treatment of retiring members as well as ensuring greater safeguards for the Fund.

The committee of Management of the Fund confirmed the change in the revaluation policy at a meeting held on 24 August 1994. The minute of the confirmation is as follows:

The secretary confirmed that the policy of revaluation had been changed from six monthly intervals to three monthly intervals. Those present at the meeting approved the change in policy; the secretary indicated that he had discussed the
The committee of Management was authorised to implement this decision in terms of the decisions taken at these meetings. This change in the policy of revaluing equities was done in terms of rule no. 10 (k), which reads as follows:

A10. Subject to the provisions of the Act the Committee shall have power to carry out the objects and purposes of the Fund in accordance with the rules, and without detracting in any way from the generality of this provision shall have the following powers:-

(11) Generally to do all such other acts or things as are, in its opinion, conducive to the attainment of the objects of the Fund."

The Committee of Management acknowledges that this should have been written into the rules but it did not realise that it was necessary in view of the powers afforded it in terms of Rule No. 10 (k). To date the rules of the Fund have not been amended but the required amendment will be formulated and registered shortly.

Rule 27 cannot be relied on, in isolation, in this case as it was agreed with the members to change the policy of revaluation. The committee of Management is confident that it has properly exercised its powers as the change in policy was for the protection of the members and the Fund, and in their opinion is an object of paramount importance. In addition the Committee of Management had a duty to act within the mandate given by the members at the AGM held on 18 March 1994.

The Committee of Management therefore disputes your contention that:

"...the said committee and/or employer have exceeded their powers in terms of the Rules, alternatively, improperly exercised their powers thereby resulting in the
With reference to your point 3.4 we wish to advise that when the revaluation policy was changed it was decided to reduce the interest on withdrawals between periods to zero.

He went on to conclude that the fund denied that the complainant’s retirement benefit had been incorrectly calculated or that the committee of management had exceeded their powers in the calculation thereof.

13. The complainant lodged his formal complaint with my office on 4 June 1999, and a copy was lodged with the respondents.

14. The complainant avers that the respondents calculated his retirement benefit in a manner contrary to the rules of the fund and in so doing have exceeded their powers in terms of the rules, or alternatively have improperly exercised their powers resulting in the maladministration of the fund.

15. He argues that, contrary to the terms of rule 27 which requires the amount of the benefit to be based on values determined at the last investigation made in terms of rule 26, being the investigation at 30 June 1998, the benefit was calculated on the basis of a valuation at 30 September 1998 and that the investigation at 30 June 1998 has been ignored.

16. The value of the full benefit as at 30 June 1998 amounted to R967,660.22 and the benefit he received was R875,384.00. In addition, he claims that he was entitled to interest at the rate determined by the committee of management from the end of June 1998 to the date of payment at the end of November 1998. He is not aware of the rate determined.
17. The complainant requests the following relief.

17.1 Payment of at least R92,276.22 plus interest from 1 July 1998 to the date of his retirement from the fund at 30 November 1998 at the rate determined by the Committee of Management in accordance with Rule 27(c).

17.2 Payment of interest thereon at the rate he could have earned on the said amount in the best interest bearing account from time to time. Alternatively, the rate presented in the Prescribed Rate of Interest Act.

17.3 Such other relief as the Adjudicator may deem appropriate.

18. The respondents initially relied on their response dated 21 May 1999 as summarised in 12 above, together with copies of minutes of the Annual General Meeting of the fund held on 18 March 1994 and minutes of a meeting of the Committee of Management held on 24 August 1994, confirming the change in revaluation policy.

19. Subsequently, in a further submission dated 31 August 1999, the complainant stated that he did not attend the Annual General Meeting on 18 March 1994 and did not recall seeing the minutes of that meeting, or of the meeting of the Committee of Management held on 24 August 1994.

20. He then went on to say that he could not accept the argument put forward in the respondents letter of 21 May 1998 that rule 10(k) takes precedence over rule 39(b), which concerns the submission of rule amendments to the Registrar for approval in accordance with the Act. He also notes that the ZAI Staff handbook of July 1996, which quotes the fund=s rules, makes no reference to the 3 months investigation.

21. The complainant then asks for the following comments to be added to the enclosures already lodged with the complaint.
It is my understanding that the Provident Fund’s Investment Managers, Allan Gray of Cape Town, provide ZAI with audited and certified investigation of the funds finances twice a year, at the end of June and December and at no other time, exactly as the Rules of the Provident Fund intimate. ZAI now, since June 1999, use this “real value” to calculate the member balance in the fund. Previously ZAI revalued the funds finance in accordance with Rule 26. Historically this revaluation was generally lower than Allan Gray’s “real value”. The new “real values” used results in a more favourable balance to the members. I understand that in the 6 months from end December 1998 to end June 1999 members balances in the fund increased by 50%, granted a reasonable portion of this figure could be from wise investment. But at least 10 to 15% can be attributed to the fact that ZAI are now accepting Allan Gray’s “real value” figure.

This then questions whether the figures issued to me in June 1998 was in fact a true value of the fund or a figure 10 to 15% less due to adjustment by the Management Committee. With this in mind the relief sought under item 8.0 in my official complaint now has to be extended to include any amount over and above the original R92,276.22, due to the difference in Allan Gray’s true value of the Fund and ZAI’s “quoted” value, plus the profits afforded to the Member’s on this amount from June 1998 to date of payment (ie. 50.33% until end June 1999). Since the original R92,276.22 must still be invested in the Provident Fund.

22. In a further submission dated 8 September 1999, Mr Johnston, in response to the complainant’s letter dated 31 August 1999, stressed that members are entitled to attend Annual General Meetings, and minutes of these meetings are available for inspection by all members of the fund. If a member chooses not to attend, he must accept that decisions taken at the meeting are binding on him.

23. He also restated the fund’s view that rule 10(k) takes precedence over rule 39(b), referring again to the following statement in the original response dated 21 May 1999.

“The Committee of Management acknowledges that this should have been written into the rules but it did not realise that it was necessary in view of the powers afforded it in terms of Rule no. 10(k). To date the rules of the fund have not been amended but the required
amendment will be formulated and registered shortly."

24. He then goes on to explain that the complainant's understanding of the revaluation process is incorrect, and that although the fund's investment managers, Allan Gray Ltd, actually produce a monthly investment report, this procedure is in no way linked to the rules of the fund. He continues:

The real value referred to by Mr Smith is the market value of the Fund’s investments, the value determined by the Fund in terms of Rule 26(i) is the book value, which has been the basis of valuation of the investments since the Fund was established. The decision to change the method of valuation of the investments was made at the AGM of the Fund, which was held on 31 March 1999, which is four months after Mr Smith retired from the Fund. This change would have increased the value of the fund at 31 December 1998 by 5.95%, the balance of 46.75% was as a result of exceptional returns achieved on investments for the period 1 January 1999 to 30 June 1999. This however, is academic as the rules governing the valuation of investments were only changed on 30 June 1999.

Issues for determination

25. What we have here is yet another example of dialogue that has deteriorated into diatribe, to the extent that by the time the dispute has reached my office, the few relevant facts have become immersed in an ocean of red herrings.

26. The single issue to be determined is, quite simply, whether the complainant received the retirement benefit to which he was entitled, or not. If this is an oversimplification then perhaps it should be expanded to:

26.1 Did the respondents act properly in their application of the rules and practices of the fund, particularly in relation to the calculation of the complainant’s retirement benefit? and

26.2 Did the complainant suffer any prejudice or financial loss as a result?
27. It is common cause that at the time in question the fund’s practice in relation to periodic investigations and the revaluing of member’s accounts in terms of rule 26 differed from the strict wording of the rules to the extend that investigations were taking place quarterly instead of half-yearly. This change in practice had been implemented as a result of a decision of the membership at an Annual General Meeting and was seen to be in the best interests of the members and the fund. However, although the decision to change was made at a meeting in August 1994, the applicable rule was not amended till June 1999.

28. The respondents claim that rule 10(k), as referred to in 12 above, provides the necessary authority to apply this change in practice and that, in fact, they were obliged to act in terms of the mandate given by the members at an Annual General Meeting. As a result, they claim, the application of rule 10(k) in these circumstances takes precedence over rule 39(b), requiring alterations to the rules to be submitted to the Registrar for approval.

29. The Act is quite clear in this respect, and in section 13, states:

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

30. Regarding alterations to the rules, the Act says in section 12(1) and (2).

(1) A registered fund may, in the manner directed by its rules, alter or rescind any rule or make any additional rule, but no such alteration, rescission or addition shall be valid.

(1) If it purports to effect any right of a creditor of the fund, other than as a member or shareholder thereof; or

(2) Unless it has been approved by the registrar and registered as
provided in subsection (4).

(2) Within 60 days from the date of the passing of a resolution for the alteration or rescission of any rule or for the adoption of any additional rule, a copy of such resolution shall be transmitted by the principal officer to the registrar, together with the particulars prescribed by regulation.

31. In terms of the rules of the fund itself, rule 39 says:

1. The Committee may, with the concurrence of the employer and subject to paragraph (b) hereunder, make such new rules, or alter or rescind any existing rules as it may think fit.

2. Notwithstanding anything to the contrary contained in these rules, any addition to or alteration in these rules shall be submitted to the Registrar for approval in accordance with the Act. Copies of all amendments or additions to these rules shall be sent to the Commissioner for approval in terms of the Income Tax Act.

3. The Committee shall either immediately upon receipt of the Registrar’s approval or at least once in every year, furnish every member with particulars of any amendments or additions to these rules.

And Rule 41(e) says:

(5) Unless otherwise specifically provided in these rules, a resolution passed at a meeting of members shall be treated as a recommendation to the Committee which shall deal with it as it may determine.
32. In summary, therefore, the fund is bound by its rules as registered with the Registrar, in terms of the Act. The rules may be amended in terms of a resolution passed by the committee of management, but no rule change will be valid until it has been submitted to the Registrar in terms of rule 39 and registered by him, in terms of the Act.

33. Although rule 10(k) does afford the fund certain powers in the application of the rules in the best interests of the members, it does not override a member’s right to have his benefits calculated strictly in terms of the rules in force at the date the benefit becomes due. It certainly does not give the fund authority to pay a lower benefit. Certainly, it cannot be relied on to effect an amendment to rules 26 and 27 in a manner circumventing the clear provision of rules 39(b) and 39(c). Moreover, the opening phrase in rule 39(b) “notwithstanding anything to the contrary contained in these rules” definitively indicates that rule 39(b) shall take precedence over any other rule, rule 10(k) included, in relation to the process of rule amendments.

34. The complainant is, therefore, entitled to have his retirement benefit calculated with reference to the investigation as at 30 June 1998 rather than the one as at 30 September 1998.

35. The question of the rate of interest to be applied in terms of rule 27(c) (see 16 above) has been raised. Could, for example, a negative rate of interest be applicable? Rule 27(c) does not specify one way or the other, but I would suggest that only a positive rate would be intended, for the following reasons.

36. It is very clear from rules 26 and 27, and confirmed by the respondents in their submission dated 8 September 1999, as quoted in 24 above, that benefit calculations are based on “book values” rather than “market values” at the applicable date. The use of book values is a common practice, which enables
funds to calculate benefits between valuation dates on a relatively smoothed basis rather than having to apply actual market values which are volatile and tend to fluctuate from day to day.

Book values do not take account of short term peaks and troughs in market values and they tend to reflect a conservative value somewhat lower than the true value of the underlying assets, except at the time of (or shortly after) a major downward market correction, when capital losses (whether realised or not) have not yet been applied to book values. Thus, capital values of member’s accounts once recorded and advised to members can be maintained between valuation dates without undue strain on the fund. The application of (positive) interest thereto allows the fund to reflect current market trends without recalculating capital values.

37. Rules 26(1) allows for such circumstances by adopting a fairly conservative approach to the calculation of the profits in terms of book value to be distributed to member accounts. It follows, therefore, that there should be no reduction in the capital value of a member’s account from one investigation date to the next, and as a result, the rate of interest determined by the committee in terms of rule 27(c) should always be a positive rate, subject to a minimum of zero in extreme circumstances.

The determination

38. The order of this tribunal is as follows:

38.1 The fund is ordered to recalculate the retirement benefit in respect of the complainant as at the date of his retirement, 30 November 1998, in terms of the rules in force at that date. The retirement benefit in terms of rule 27 will be based on, and equal to no less than, the value arrived at by applying the value of the complainant’s accumulated contributions as determined at 30 June 1998 and advised to the complainant at the time. The interest rate
applicable in terms of rule 27(c) must be determined by the committee of management in accordance with their practice at that time, reflecting the actual experience of the fund at the time.

38.2 The fund shall pay the difference between the benefit so calculated and the gross benefit indicated on the statement of withdrawal benefit on termination of service dated 7 December 1998, to the member, together with interest thereon at the same rate prescribed from time to time in respect of a judgement debt in terms of section 2 of the prescribed rate of interest Act of 1975, for the period from 30 November 1998 to 30 November 1999 and less tax deducted in terms of a tax directive to be obtained by the fund from the complainant’s Receiver of Revenue.

38.3 The net balance of benefit after deduction of tax shall be paid to the complainant by the fund no later than six weeks after the date of this determination.

Dated at CAPE TOWN this 2nd day of November 1999.

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John Murphy
Pension Funds Adjudicator