IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO.: PFA/WE/330/99/AS

In the complaint between:

J J FRIESLAAR                                         Complainant

and

SAFICON-BOUMAT PENSION FUND                           Respondent

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

Introduction

This is a complaint lodged with the Pension Funds Adjudicator in terms of section 30A(3) of the Pension Funds Act of 1956.

The complainant is Mr J J Frieslaar an erstwhile member of the respondent and former employee of Waud and Blackman a participating employer in the fund.

The respondent is the Saficon-Boumat Pension Fund a pension fund duly registered in terms of the Pension Funds Act 1956.

The complainant, alleging that he had been underpaid by the respondent in terms of the rules of the respondent on his retiring entered into correspondence with the respondent in order to negotiate that the amount alleged to be outstanding by him, be paid to him by the respondent. The parties were unable to resolve the dispute and the complainant duly lodged a written complaint with the Pension Funds Adjudicator on 9 February 1999.
No hearing was held in this matter, but a report was placed before me by investigator, Antonia Simmons. Accordingly, in determining this matter I have relied on the documents and report placed before me and the exchange of correspondence. Having completed my investigations I have determined this complaint as follows and for the reasons set out herein.

The factual background and arguments

The complainant was employed by Waud and Blackman, a participating employer in the respondent, from 1951 until he retired in 1998. He was a member of the respondent for the duration of his period of employment. Regular payments were paid into the fund for the relevant period.

In 1990 the complainant was judged to be medically unable to perform his own occupation or any similar occupation taking into account his education, experience and training. At this time his monthly salary was R3,000.00 and he was granted a monthly benefit from the Saficon-Boumat Benefit (Disability) Fund of R2,100.00 (being 70% of his salary) in accordance with the rules of the benefit fund. This benefit was payable net of taxation until he recovered from his disability, died, retired or attained the age of 65 whichever occurred first. The trustees of the benefit fund reviewed the monthly benefit and inflationary increases were granted. Shortly before the age of 65 the monthly benefit had increased to R4,427.82.

During the period that the complainant was in receipt of a disability benefit, his membership of the respondent was maintained. Contributions to the respondent, both member's and employer's were paid by the Benefit Fund in addition to the benefit paid to the complainant and in accordance with the rules of the Benefit Fund.

The complainant's pension fund salary (R3,000.00 per month at May 1990) was increased at the same time and rate as increases to the monthly benefit from the benefit fund.
During the period of maintained membership his salary increased from R3,000.00 per month in 1990 to R6,704.99 per month in 1998.

The complainant considered retiring early, making an application to retire in 1995 when he was aged 62 years. He was, however, according to his submissions advised that he would be “penalised” if he were to retire at that age and was encouraged to delay his retirement until he had reached the age of 65 at which stage his pension benefit would be greater. He accordingly delayed his date of retirement to take effect from 31 October 1998 by which time he had attained the age of 65 being the “retirement age” stipulated in terms of the rules of the respondent.

In July 1998 Wynne-Jones and Company were contacted by the complainant’s ex-employer who intimated that the complainant was concerned that his disability benefit was due to cease and that he believed that his pension benefit would reduce dramatically. Wynne-Jones responded to the communication in writing detailing the pension benefits to which he would be entitled in terms of the rules of the respondent.

There is no evidence to indicate that the complainant ever had sight of this letter or had the contents and implication thereof explained to him.

The complainant retired on 31 October 1998 and the rules of the respondent which became applicable to him were rules 29(a) and 28(a) in terms of which his full pension was calculated. The relevant rules of the respondent read as follows:

29. RETIREMENT AT THE RETIREMENT AGE

(a) a member who has attained the retirement age shall be entitled to a pension calculated in terms of rule 28. Such pension shall commence with effect from the retirement date irrespective of whether or not the member remains in the service after that date provided that if the member so elects, and the committee and the employer agree thereto, the commencement of the pension may be deferred until a
28. PENSION

(a) Members of the Fund who have not been contributing members of another fund during their period of membership of the fund:

Subject to the provisions of these rules, the pension granted to such a member who is retiring shall be equal to N/45th of the member's pensionable salary, where N is the member's pensionable service in years and fractions of a year, taking into account only completed months.

(d) The pension shall be payable monthly in arrear during the lifetime of the pensioner, the first payment falling due on the last day of the month following that in which the event occurs upon which the pension is payable. The last payment shall be made at the end of the month in which the member dies, subject to any other benefits which may be payable under these rules.

(e) Each pension payable in terms of the rules shall be paid from the Fund except that, at the request of the member on his retirement, or a pensioner at any time during retirement, the Committee may direct that an annuity be purchased from an insurer or any other approved pension or annuity instrument. The amount applied to purchase such annuity shall be all, or such part as may be requested by the member or pensioner as the case may be, of the accrued service actuarial reserve as determined by the actuary in respect of the member or pensioner.

32 BENEFITS PAYABLE ON DEATH
(c)(ii) If a pensioner shall die leaving a widow as defined, the widow shall be entitled to a pension equal to seventy percent of the pension the pensioner was receiving at the time of his death. Such pension shall be payable monthly in arrear during the lifetime of the widow, the first payment falling due on the last day of the month following that in which he pensioner dies. The last monthly payment shall be made at the end of the month in which the widow dies...

36. COMMUTATION OF PENSION AND OPTIONS ON RETIREMENT

(a) At the request of a retiring member the committee may, in its absolute discretion, commute for a lump sum at date of retirement not more than one-third of his pension or the whole of his pension if this is permitted in terms of the prevailing income tax legislation. If the member shall commute the whole of his pension then no widows pension will be payable in terms of rule 32(c)(ii).

(c) The amount of the lump sum in terms of sub-rule (a) and (b) shall be decided by the committee acting upon the advice of the actuary.

“PENSIONABLE SALARY”

Shall mean the member's average salary over the three years of service immediately prior to the retirement date, or if greater, the member's average salary over any other period of three consecutive years of service, provided, however, that should the member's salary decrease at any time, and should the member wish to have his pension related to the three consecutive years of service which produced the highest pensionable salary he must give written notice to this effect and agree to pay contributions in respect of his salary before reduction and provided further that if on the retirement date, a member is in receipt of a disablement income benefit from the benefit fund, then his pensionable salary shall be equal to his salary or such higher salary as the committee, in its absolute discretion, shall decide.
“RETIREMENT AGE”

Shall mean the age of 65 years.

“SALARY”

In any year shall mean the annual total of the basic salary or wage, production bonus received during the twelve months preceding the first day of April or October of that year, or the annual equivalent of the production bonus received during the actual period of service if this does not extend to the full twelve months preceding the said first day of April or October and average annual commission earned during the three years, or the actual period of service if this is shorter than three years, previous to the said first day of April or October plus such additional amounts as the Committee, in its absolute discretion after consultation with the actuary and the employer, shall decide. In the case of a member who is in receipt of a disablement income benefit from the benefit fund salary in any year shall mean the salary on which the disablement income benefit received by the member is based or such higher salary as the committee, in its absolute discretion, shall decide. For the purposes of these rules a change in salary will take effect on the first day of the month on which a change occurs in the remuneration on which the salary is based.

The calculations were duly effected where N was calculated at 47 years 10 months (1 January 1951 to 31 October 1998) and “pensionable salary” was R72,131.63 per annum being the member’s average “salary” during the last 36 months of membership. The complainant's full pension was thus R6,389.44 per month (being 47 and 10/12 x 1/45 x R72,131.63 ) 12).

In terms of rule 36(a) the complainant elected to commute 1/3 of his pension for a lump sum. The amount of the lump sum was determined as R305,180.13, the calculation was
based on certain tables utilised by the respondent. One third of the annual pension was multiplied by a specified rate according to age. This commutation factor was obtained from the table and in the instance of a 65 year old married male such as the complainant was 11.94200. This amount was paid to the complainant, less the deduction for tax of R25,293.64, on 11 November 1998. The balance of the benefit due to the complainant (R4,259.63 per month) would then have been payable to him by the respondent for the rest of this life with provision for increases at the trustees discretion and provision for the pensioner's spouse.

The complainant, however, elected that in lieu of a pension being paid from the respondent an annuity be purchased from another approved annuity instrument in terms of rule 28(e). The respondent agreed to the request, which took the form of a facsimile proposal form from Investec dated 8 September 1998 and which indicated that the correspondent wished to transfer the 2/3rds portion of his pension to the Investec Life Annuity. The release was effected in terms of rule 28(e) in accordance with which the accrued service actuarial reserve as determined by the actuary was payable. The actuary determined the actuarial value reserve of the full pension at R890,286.00 of which R305,180.13 had already been paid out in cash. The balance of the actuarial reserve value which amounted to R504,106.00 was deposited into Investec's bank account on 29 October 1998.

The complainant objected to the quantum which was paid to Investec stating that a further R106,254.26 was due to him by the respondent. The complainant directed a letter to Wynne-Jones & Co on 23 November 1998 noting his dissatisfaction and enquiring as to why the amount of R106,254.26 should have been deducted from his benefit.

No discussions were held between the complainant and respondent. The complainant did not seek advice directly from the respondent regarding the prudence of his election nor did he seek a quotation of the amount available to purchase an annuity outside the respondent. The respondent did not seek to advise the complainant, to assist him in his
election or to supply him with details of quotations or the implications of the various options available to him.

The Investment Linked Life Annuity which was purchased by the complainant from Investec provides him with an investment in unit trusts. There is no undertaking or promise by Investec that a set or definite amount will always be forthcoming. The investment is market linked and is dependent upon the market at any given time. There exists an obligation to draw an income between 5% and 20% of the whole which can be paid monthly, quarterly or annually. The higher the percentage drawn by the investor the greater the danger of termination of the available funds. With decreasing capital the annual annuity payments would decrease proportionately. No provision is made for a widow save insofar as a beneficiary may be nominated.

The complainant objects to the fact that an amount of R106,254.26 was “deducted” from the due to him. He submits that this is unreasonable and that the amount should be refunded to him. He calculates that if at retirement 1/3rd of the amount due to him was the amount of R305,180.13 (which was the lump sum paid to him) the annuity portion should have been R610,306.26. He calculates this amount by multiplying the 1/3 cash portion allocated to him by two, thus utilising the 1/3 lump sum as the basis from which his calculations are effected.

The respondent argues, however, that the cash element of R305,180.13 which was allocated to the complainant as his 1/3 lump sum was calculated before the complainant had indicated that he wish to proceed in terms of rule 28(e) and that the said lump sum in fact exceeded the 1/3 of the actuarial reserve value. The lump sum was calculated in terms of the rule together with standard commutation figures used for this purpose. The table of these commutation factors has been supplied by the respondent. As indicated above this calculation was N(in complainant’s instance 47.8333)/45th x average salary for past three years ) 3 x commutation factor (for 65 year old married man 11.94200).
The manner in which the accrued service actuarial reserve value was calculated, however, was:

accumulated contributions x factor 1 + 1/45 x pensionable service x salary at retirement x factor 2.

In the case of the complainant who was aged 65 at the date of the calculation,

factor 1 = nil;  
factor 2 = 9.452;  
Pensionable service = 47 years 10 months; and  
salary at retirement = R80,459.83.

The actuarial reserve value was therefore calculated as

1/45 x 47.8333 x 80459,83 x 9,452 = R808,389.00.

In the case of the complainant a slightly higher value of R809,286.00 was derived because his value was calculated by the actuary directly from the valuation programmes. It had been the practice of the respondent in the past to maintain the quoted cash amount and to utilise the balance to purchase the annuity. Since the actuarial reserve value of the complainant's full pension was R809,286.00 the balance available to be transferred was the sum of R504,106.00 and was not twice the cash value.

The respondent submits that since the complainant elected to withdraw his actuarial value, it has acted in accordance with the rules and had awarded the correct amount to the complainant. Despite this the respondent, if the complainant repays prepared to reinstate him and to provide benefits in accordance with the respondent's rules which would be R4,259.63 per month with provision for increases at the trustee's discretion and provision for the pensioner's spouse.
The respondent has also notified my investigator, that due to the unbundling of the group, the fund will terminate probably at 31 December 1999. As part of the termination process pensions will be purchased by the fund with a leading life assurance company. The fund, moreover, has a surplus of assets over liabilities and the fund’s pensioners will participate in an allocation of the surplus. The precise effect of the surplus distribution is not yet known.

After the respondent indicated its willingness to reinstate the complainant my investigator communicated telephonically on several occasions with Mr Kilpatrick of Wynne Jones & Co, the administrators of the fund. Mr Kilpatrick confirmed the offer and was most helpful in explaining the financial implication for the complainant of the return to the fund. Mr Kilpatrick also communicated with the actuary Mr Brown of Alexander Forbes who supplied details of the actuarial calculation applied to the complainant’s benefits. Mr Brown also explained the calculations, telephonically to my investigator.

The complainant attended at my office on several occasions and discussed the matter further with my investigator. The options available to the complainant were explained to him as was the manner in which the actuarial calculations applicable to his benefit had been effected. He was further informed that if he were to elect to return to the fund he would be entitled to share in the impending surplus distribution. An offer was made by Mr Kilpatrick for the complainant to telephone him and discuss the issue should he so wish. The complainant took advantage of this offer and discussed the matter directly with Mr Kilpatrick. Thus fully informed of the facts the complainant was given the option of electing either to return to the fund with the attendant consequences or to retain his benefit in the annuity purchased with Investec.

After protracted deliberation the complainant decided not to return to the fund but rather to leave his benefit in the annuity with Investec. The complainant has therefore requested
me to make an order regarding the sum of R106,254.26 which he continues to submit is due and owing to him by the respondent.

**Determination**

It is clear from the evidence before me that no adequate consultation was held with the complainant by the respondent prior to his first election and decision to transfer his 2/3 benefit to an Investec annuity. At this stage, therefore, the respondent failed in its fiduciary duty to the complainant in that it did not adequately appraise him of the options available to him or explain to him the consequences of his election. The respondent has, however, more than adequately made up for this initial omission. Mr Kilpatrick representing the respondent has done everything in his power to ensure that the complainant is properly and correctly informed advised and encouraged with regard to the correct election of option. Whereas I might have ordered that the respondent was to supply the complainant with full details and implications of the options available to him and grant the complainant once again the opportunity to make an election, in the light of the initiative taken by the fund such order has clearly become unnecessary. The complainant has made his election for the second time while being fully and properly appraised of the financial implications of such an election.

It is prescribed by the Income Tax Act 58 of 1962 as amended, in terms of the definition of “pension fund” that a pension fund may not be approved, unless, inter alia

(i) The rules of the fund provide

(ii) The rules of the fund provide

(dd) that not more than 1/3 of the total value of the annuity or annuities to which any employee becomes entitled, may be commuted for a single payment, except where the annual amount of annuity or annuities does not exceed R1,800.00 or such other amount as the Minister of Financial may from time to time fix by notice in the Gazette;

The respondent has, therefore, by paying to the complainant what it alleges to be a sum greater than the 1/3 of the total available, possibly contravened this provision of the
Income Tax Act. The respondent states in its written representations that “although the cash element exceeded 1/3 of the actuarial reserve value the practice of the fund in the past was to maintain the quoted cash amount and utilise the balance to purchase an annuity”.

Such a practice is questionable and should be reassessed in all instances in the future in order that the respondent adequately complies with the provisions of the Income Tax Act. It does not, however, follow that as a result of the respondent paying out more than it should have done as a 1/3 commutation, it automatically follows that the respondent therefore owes the complainant a correspondingly higher amount. The amount due to the complainant is to be calculated in terms of the rules of the fund, reasonable and fair actuarial practice and in accordance with the provisions of the Pension Funds Act and the Constitution.

The issue which remains to be addressed relates to the manner of calculation of the benefit, the reason for the discrepancy in quantum of benefit if any, an enquiry as to whether the lump sum was in fact more than 1/3 of the fair and reasonable benefit due to the complainant and whether the method used by the actuary was an acceptable method and within the bounds of normal actuarial practice.

In calculating the 1/3 available for payment to the complainant the respondent utilised commutation factors from a table supplied by their actuary. As indicated above and in terms of rule 28(a) together with necessary commutation factor, which in the complainant's case is 11.94200, he being 65 years of age at the date of calculation the calculation was effected as follows:

\[
\frac{47.8333}{45} \times R72,132.00 \times 3 \times 11.94200
\]

Since the complainant elected not to remain in the fund but rather to withdraw entirely it then became necessary for the actuary to calculate the accrued service actuarial reserve
as stipulated in the relevant rule of the respondent being rule 28(e). This calculation too was effected based on precalculated factors. As indicated above this was accumulated contributions x factor 1 + 1/45 x pensionable service x salary at retirement x factor 2 where factor 1 was nil and factor 2 was 9,452 for the complainant.

The trustees made a decision to accept and adopt these methods of calculation and these assumptions for the purposes this fund. The complainant was given a clear option of staying within the fund in which case the appropriate calculations and assumptions would be used in order to arrive at a value or alternatively to withdraw his total benefit in which case a different method of calculation would be used.

The trustees acted in accordance with the rules of the fund. The complainant was fairly treated as he was given the option to elect to remain within the fund or to leave the fund. The actuarial calculation in respect of the complainant are correct and moreover the methods of calculations and assumptions are fair, reasonable and within the bounds of normal actuarial practice. The complainant is therefore not owed R106,254.26 by the respondent or any other amount.

The complainant is accordingly dismissed.

DATED at CAPE TOWN this 30th day of AUGUST 1999.

____________________________________
John Murphy
Pension Funds Adjudicator