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GENERAL NOTICE

NOTICE 1867 OF 2001

NATIONAL TREASURY

PROPOSED AMENDMENT OF PENSION FUND REGULATIONS

1. I, **TREVOR ANDREW MANUEL, MP**, Minister of Finance, intend amending the Pension Fund Regulations made in terms of section 36(1) of the Pension Funds Act, 1956 (Act No 24 of 1956), as set forth in the schedule hereto.
2. Interested persons and institutions are invited to submit written representations on the proposed amendment by no later than 6 September 2001.
3. All submissions must be addressed to:

Mr C Malan
National Treasury
Private Bag X115
Pretoria
0001

You can contact Mr Malan at:

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TA MANUEL, MP
MINISTER OF FINANCE
DATE: 17 August 2001

SCHEDULE TO REGULATIONS

Exposure Draft-Regulations required in terms of section 15B(3) of the Pension Funds Act, 1956 (Act No. 24 of 1956).

The principles embodied in the exposure draft-Regulations are as follows:

(1) Retrospective review should not place undue strain on the retirement funding system.

The retrospective review of benefits paid to former members should not place undue strain on the retirement funding system. By this, we mean that only existing actuarial surplus should be apportioned, unless it can be demonstrated that the employer has utilised actuarial surplus previously in an improper manner, in which case a deficit may be created to a maximum of the present value of such surplus utilised improperly for the benefit of the employer. The latter amount is defined as E in subregulation (3), and represents the amount corresponding to

- Benefit improvements for decision makers to a level not enjoyed by the other members.
- Additional pension to selected members in lieu of the employer's obligation to subsidise medical costs after retirement.
- Recognition of prior pensionable service for selected members or members transferred into the fund, in either case without payment into the fund of the cost of this past service.

The employer may not be required to pay into the fund more than the deficit created during the apportionment of surplus to former members and pensioners, with a maximum of E.

(2) How far back should the board of a fund go in looking at past transfers, conversions and retrenchments?

The board must look at all transfers, retrenchments and conversions from 1 January 1980 onwards. If this is not done, the conversions from employer sponsored defined benefit funds to negotiated defined contribution funds will not be included.

There are escape clauses if the board satisfies the registrar, after taking steps to try to construct the data or advertise for potential beneficiaries, that it is impossible to obtain sufficient data to enable calculation. Advertisement at the employer and in the area of employment will only be required in the case of large transfers, retrenchments or conversions (ie. more than the higher of 50 members and 10% of the members at the end of the previous financial year) where the data is not available.

(3) Which transfers, conversions and retrenchments should be included?

All significant transfers, conversions and retrenchments should be reviewed.

"Significant" means at least 10% of the membership at the start of the year must have been affected by the transfer, conversion or retrenchment, provided that at least 50 members were affected. Otherwise, for example, in a fund of 20 members, the retrenchment of 2 employees would cause review.

(4) How much should the former members get?

Top former members up to the lower of

(a) The minimum benefit defined in sections 14A and 15K (which is the fair value equivalent of the present value of the benefits foregone in terms of past service determined using a prescribed set of assumptions), and

(b) The accrued actuarial liability multiplied by the ratio of the fair value of the assets to the actuarial value of the assets (being the fair value of the assets in the fund reserved in respect of the transferring members prior to the transfer).

The former members should get this as a prior charge against surplus.

(5) The remaining surplus should then be apportioned by the board on an equitable basis amongst stakeholders.

Once this has been done, the balance of the actuarial surplus can be shared between active members, former members and the employer in any way that seems equitable to the board. The requirement that members be told of the apportionment, and have an opportunity to object, will cause an effective negotiation of this sharing between active members and the employer.

(6) What does the board of a fund do if the top up in paragraph (4) puts the fund into a deficit situation?

If there is not sufficient surplus in the fund, after adjustment by E in line with paragraph (1) above, to allow the top up in paragraph (4), then the top up must be proportioned down.

More minor issues are as follows:

(7) A formula approach is provided both for small and large funds which will automatically be deemed to be equitable, if used. This will reduce the cost of the exercise.

(8) The board may not exclude transfers out if the employee concerned is still employed, even though other former members who are no longer employed are excluded because of a lack of data. This will prevent a paucity of data in respect of former employees denying participation to current employees who no longer belong to the fund.

(9) A new subregulation is added to clarify what the trustees should do if the funding position has changed significantly over the period of the exercise.

Exposure Draft-Regulations required in terms of section 15B(3) of the Pension Funds Act, 1956 (Act No. 24 of 1956)

Matters, envisaged in section 15B(3) of the Pension Funds Act, 1956, to be considered by the board of a fund in apportioning accrued actuarial surplus following the date of commencement of the Pension Funds Second Amendment Act, 2001.

(1) When actuarial surplus is to be allocated between members, former members, and the employer using the process set out in section 15B of the Act, the board of the relevant fund, with the assistance of an actuary, must examine the financial history of the fund, and identify all transfers, conversions, and retrenchments that took place after 1 January 1980:

Provided that the board may exclude from participation any transfers, retrenchments and conversions in respect of which the board satisfies the Registrar that insufficient records are available to enable the additional benefits that may be due to such former members to be calculated, after the board has taken reasonable steps —

- to obtain such records from the administrator,
- to construct such records from the records of the employer, and
- to obtain such records from the potential claimants themselves following an advertisement in the area where the former members used to work:

Provided, further, that, where former members, who participated in an exercise for the transfer, conversion or retrenchment within a financial year of at least the greater of 50 members and ten per cent (10%) of the membership of the fund at the end of the previous financial year, are to be excluded because of the unavailability of sufficient records to enable their inclusion in the apportionment, the fund must accord such former members as are to be excluded at least six (6) months to come forward and provide sufficient information to enable the calculations to be performed after advertisement on the employer's premises and in the area where the former members used to work:

Provided, further, that the board may not exclude existing employees who were former members of the fund from participation.

(2) In all cases not covered under subregulation (4), the actuary must establish a broad analysis of the actuarial surplus by source starting with the actuarial surplus existing at the statutory valuation coincident with or closest preceding the earliest event identified in subregulation (1) resulting in the inclusion of former members in the apportionment; such analysis must quantify the value as at the surplus apportionment date of the following:

A represents the total for all events identified in subregulation (1) of the minimum benefit value as at the date of the event less the amount actually transferred or paid, subject to a minimum of zero, accumulated at the rate of investment return earned by the fund from the date of the event up to the apportionment date, nett of expenses associated with the investment of the assets of the fund including retirement fund tax: Provided that this minimum benefit value will represent the lower of

- the amount obtained by applying the formula as at the date of commencement of the Pension Funds Second Amendment Act, 2001, as described in sections 14A and 15K (or some reasonable approximation of this), and
- the accrued actuarial liability multiplied by the ratio of the fair value of the assets divided by the actuarial value of the assets as at the date of transfer, conversion or retrenchment, where all values are determined using the method and assumptions set out in the statutory actuarial valuation coincident with, or immediately prior to, the event;

B represents the nett amount of actuarial surplus accumulated to the date of apportionment arising from

- investment returns earned on the actuarial value of assets corresponding to liabilities in respect of active members, nett of expenses associated with the investment of the assets of the fund including retirement fund tax, where the investment returns earned have differed from the rate assumed by the actuary, and where "active member" means a member who contributes or in respect of whom the employer contributes to the fund;
- salary increases which have differed from the rate assumed by the actuary; and
- adjustment to the method of valuation of all the assets less that portion of such adjustment which is related to assets backing pensioner and deferred pensioner liabilities and which is included under D: Provided that, if B is negative, B shall be increased to zero;

C represents the cost of benefit improvements awarded to active members, with a maximum of B;

D represents the nett amount of actuarial surplus required to increase pensions and deferred pensions to the minimum levels required in terms of sections 14A and 15K of the Act;

E represents the present value at the surplus apportionment date of surplus utilised for the benefit of the employer during the period of the analysis, where such utilisation may not have been approved if the board of the fund had been constituted in terms of section 7A, and the board had been directed that the utilisation of surplus should be negotiated between the stakeholders and was not automatically at the disposition of the employer. E must include:

- any benefit improvements awarded to senior management in excess of the level of benefit improvement that would have applied had they been ordinary members;
- the cost to grant pensionable service to members that transferred into the fund during the period in excess of the amount that could be secured by the fair value of the assets transferred into the fund, using the actuarial assumptions and method applicable at the statutory actuarial valuation coincident with, or immediately preceding, the transfer of the members;
- the cost of any increases in pensions or deferred pensions granted to members or former members on condition that the members or former members relinquish any right to any subsidy by the employer of their medical costs after retirement, unless such increases were approved by a board properly constituted in terms of section 7A and with the informed consent of the members or their representative trade unions;
- the value of any contribution holiday enjoyed by the employer after the commencement date of the Act.

F represents the total amount of actuarial surplus to be allocated, as established by the board of the fund after the board has set aside such amounts as it deems reasonable in contingency reserve accounts, before adjusting the actuarial surplus by the amount E;

K represents the lower of $(E + F) / (A + B - C + D)$ and 1;

M represents the member contributions accumulated with the valuation rate of interest;

T represents the total contributions paid into the fund accumulated with the valuation rate of interest;

e represents the expenses, excluding any expenses deducted in the calculation of B and D, accumulated with the valuation rate of interest:

Provided that the actuary may use the information contained in the statutory valuation reports as a basis for his or her calculations rather than attempting to calculate these numbers from source data.

(3) In all cases not covered under subregulation (4), the board of the fund shall then apportion surplus in terms of section 15B(3)(c) and (d) in such a way that former members should get at least $Q1 = A \times K$, pensioners and deferred pensioners should get at least $Q3 = D \times K$, where A, D and K represent the terms defined in subregulation (2), and the balance of the surplus (namely $F + E - Q1 - Q3$), where F and E are defined in subregulation (2), should be split in an equitable manner between the active members, who receive an amount described as Q2, and the employer who will receive $F + E - Q1 - Q2 - Q3$ by transfer into the employer surplus account. Such apportionment shall be conducted by the board in the exercise of their fiduciary duties towards all stakeholders.

(4) Where the conditions set out in paragraph (a) are satisfied, the fund may elect to distribute actuarial surplus between members, former members and the employer as set out in this subregulation, in which case subregulations (2) and (3) shall not apply.

(a) The actuarial surplus is less than one (1) million Rand at the surplus apportionment date, the financial history of the fund does not reveal a significant change in the financial position following the transfer out, or retrenchment, of members in the past, and the employer has not utilised a significant amount of surplus in the past. In this context, "significant" shall mean an amount with a value at the surplus apportionment date of one million Rand or more.

(b) Such amount should be deducted from the actuarial surplus apportioned to members and distributed to former members (identified in terms of subregulation (1)) as will increase the benefit paid to former members to the lower of

- the amount obtained by applying the formula as at the date of commencement of the Pension Funds Second Amendment Act, 2001, as described in sections 14A and 15K (or some reasonable approximation of this), and
- the accrued actuarial liability multiplied by the ratio of the fair value of the assets to the actuarial value of the assets, where values of assets and liabilities are determined using the method and assumptions set out in the statutory actuarial valuation coincident with, or immediately prior to, the event.

Such amounts should be accumulated to the calculation date using the investment return earned by the fund.

Pensions and deferred pensions should be increased to the minimum level defined in the Act.

In total the former member, pensioner and deferred pensioner amounts due shall be referred to as "modified" benefits. If there is insufficient actuarial surplus to achieve this increase to "modified benefits", all "modified benefits" shall be proportionately reduced to equal the amount of actuarial surplus available.

(c) The residual actuarial surplus will be split in proportion to the accumulated value of the contributions by members and the employer, respectively, less expenses, where contributions are rolled up to the calculation date using the investment return earned by the fund, nett of expenses which should reasonably be deducted from the investment return (such as the expenses of investment management and any retirement fund tax). This will give rise to an employer portion and a member portion of actuarial surplus. The employer portion will be credited to the employer surplus account. The member portion will be further apportioned as set out in paragraph (d).

(d) The member portion of the actuarial surplus should then be distributed between active and former members in proportion to their respective accrued liabilities at the calculation date.

(5) Where the conditions of subregulation (4)(a) are not applicable or the fund elects to use this subregulation, the Registrar and the specialist tribunal shall regard as equitable a distribution according to the following formulae, in which items A to F, K, M, T and e represent the terms defined in subregulation (2):

(a) former members get at least $Q1 = A \times K$;

(b) existing members, by or in respect of whom contributions are currently being paid, get at least $Q2 = (B - C) \times K \times M / (T - e)$: Provided that, where there has been a material reduction in the membership of the fund across the period, Q2 will relate to surplus due to current and former members, and the board should determine what portion of this was earned during the period in which former members participated in the fund, in which case such amount would then be deducted from Q2 and added to Q1;

(c) pensioners and deferred pensioners get at least $Q3 = D \times K$;

(d) the balance of the surplus, namely $F - Q1 - Q2 - Q3$, should be credited to the employer surplus account.

(6) Where there has been a material change in the funding ratio (that is the ratio of the actuarial value of the assets to the value of the accrued liabilities) over the period of the analysis, the board of the fund should consider the financial position of the fund at the effective date of each significant transfer or retrenchment exercise, perform a distribution as noted above, and then accumulate the amounts forward at the investment return earned by the fund, recording the distribution that they deem appropriate for each such significant transfer or retrenchment exercise. This may better inform the board as to the equity of any past distribution of surplus, transfers or retrenchment exercises, relative to the financial position of the fund at the time of such exercises.

(7) If the employer surplus account is then in deficit (because $Q1 + Q2 + Q3$ exceeds F), the employer will be required to agree with the trustees how the deficit will be amortised: Provided that, on termination of the fund before this resulting deficit is funded, as with any other deficit, the deficit will be regarded as a debt of the employer; and

(8) The board of trustees must then equitably apportion Q1, Q2 and Q3 as determined in subregulation (3) amongst the appropriate stakeholder group.

(9) Where former members to whom the board apportions some share of the surplus cannot be traced, the share of surplus apportioned to such former members shall be treated in the same manner as any unclaimed benefits are treated in the fund.

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